Chapter 12(b)

Other Topics-Voluntary Fiduciary Correction of Prohibited Transactions

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INTERNAL REVENUE SERVICE
TAX EXEMPT AND GOVERNMENT ENTITIES

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Overview

Introduction

There have been three publications issued in the last year, which affect what an agent should look for when reviewing prohibited transactions under Code Section 4975. The publications issued are:

- Voluntary Fiduciary Correction (VFC) Program of the Department of Labor
- Prohibited Transaction Class Exemption 2002-51
- Internal Revenue Service Announcement 2002-31

Announcement 2002-31-proposed class exemption

Introduction

Announcement 2002-31 was released March 27, 2002, as a companion document to the release by the U.S. Department of Labor (the "DOL"), of a proposed class exemption from the prohibited transaction rules (Application No. D-10933) with respect to four of the transactions enumerated in its Voluntary Fiduciary Correction ("VFC") Program. (The DOL's permanent VFC program and proposed class exemption from the prohibited transaction rules were published in the March 28, 2002, issue of the Federal Register and Announcement 2002-31 was published in the April 15, 2002, issue of the Internal Revenue Bulletin.)

The announcement states that when finalized, the proposed class exemption will provide relief from the application of the excise taxes described in IRC Sections 4975 (a) and (b). The exemptions apply only with respect to four of the transactions enumerated in the VFC Program that would otherwise have resulted in violations of IRC Sections 4975(c)(1)(A) through (E).

4 enumerated transactions that otherwise would have been prohibited transactions

The enumerated transactions were:

1. The failure to transmit participant contributions to a pension plan (using DOL's definition of a pension plan) within the time frames described in the DOL's regulation at 29 CFR section 2510.3-102, (VFC Program, section 7.A.1.). (The failure to transmit participant loan repayments to a pension plan within a reasonable time after withholding or receipt by the employer was added when the class exemption became effective on November 25, 2002.)
2. A loan at a fair market interest rate to a party in interest with respect to a plan. (VFC Program, section 7.B.1.)
3. A purchase or sale of an asset (including real property) between a plan and a party in interest at fair market value. (VFC Program sections 7.C.1. and 7.C.2.)
4. The sale of real property to a plan by the employer and the leaseback of the property to the employer, at fair market value and fair market rental value, respectively. (VFC Program, section 7.C.3).

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Announcement 2002-31-proposed class exemption, Continued

Section 4975-

IRC Section 4975(a) imposes an initial excise tax of 15 percent of the amount involved in a prohibited transaction on the disqualified person(s) who participated in the prohibited transaction. IRC Section 4975(b) imposes an additional excise tax of 100 percent of the amount involved in a prohibited transaction on the participating disqualified person(s) if the prohibited transaction is not corrected within the Taxable Period (as defined in IRC Section 4975(f)(2)).

Section 4975-definition of prohibited transaction (4975(c))

Under IRC Sections 4975(c)(1)(A) through (E), the term "prohibited transaction" means any direct or indirect:

(A) sale or exchange, or leasing, of any property between a plan and a disqualified person;

(B) lending of money or other extension of credit between a plan and a disqualified person;

(C) furnishing of goods, services, or facilities between a plan and a disqualified person;

(D) transfer to, or use by or for the benefit of, a disqualified person of the income or assets of a plan; or

(E) act by a disqualified person who is a fiduciary whereby he deals with the income or assets of a plan in his own interest or for his own account.

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Announcement 2002-31-proposed class exemption, Continued

Conditions for eligibility for the proposed exemption

To be eligible for the proposed class exemption, the following conditions in the proposed class exemption must be met:

1. With respect to the first transaction, the contributions must have been transmitted to the plan not more than 180 calendar days from the date the amounts were received by the employer or the date the amounts otherwise would have been payable to the participant in cash.
2. With respect to the transactions described in transactions 2, 3 & 4, the plan assets involved in the transaction, or series of related transactions, did not, in the aggregate, exceed 10 percent of the fair market value of all the assets of the plan at the time of the transaction.
3. With respect to the transactions described in transactions 3 & 4 , the fair market value of any plan asset involved in the transaction was determined in accordance with section 5 of the VFC Program.
4. The terms of a transaction described in Sections 2, 3, or 4 were at least as favorable to the plan as the terms generally available in arm's-length transactions between unrelated parties.
5. With respect to any enumerated transaction, the transaction was not part of an agreement, arrangement or understanding designed to benefit a party in interest.
6. With respect to any enumerated transaction, the applicant has not taken advantage of the relief provided by the VFC Program and the exemption for a similar type of transaction(s) identified in the current application during the period, which is three years prior to submission of the current application. (The three-year rule was modified effective November 25, 2002. See, Section II.F.(2) of Exhibit I.)
7. The applicant has met all of the applicable requirements of the VFC Program.
8. The Employee Benefits Security Administration (EBSA) (formerly, the Pension and Welfare Benefits Administration) has issued a no action letter to the applicant pursuant to the VFC Program with respect to the transaction.

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Announcement 2002-31-proposed class exemption, Continued

Conditions for eligibility for the proposed exemption (continued)

9. Written notice of the transaction(s) for which the applicant is seeking relief pursuant to the VFC Program and the proposed class exemption, and the method of correcting the transaction, must be provided to interested persons within 60 calendar days following the date of the submission of an application under the VFC Program. A copy of the notice must be provided to the appropriate Regional Office of the U.S. Department of Labor, EBSA within the same 60-day period, and the applicant must indicate the date upon which notice was distributed to interested persons.
10. Plan assets may not be used to pay for the notice. The notice must included an objective description of the transaction and the steps taken to correct it, written in a manner reasonably calculated to be understood by the average plan participant or beneficiary. The notice must provide for a period of 30 calendar days, beginning on the date the notice was distributed, for interested persons to provide comments to the appropriate Regional Office. The notice must include the address and telephone number of such Regional Office. The notice must be given in a manner that was reasonably calculated, taking into consideration the particular circumstances of the plan, to result in the receipt of such notice by interested persons, including but not limited to posting, regular mail, or electronic mail, or any combination thereof. The notice must inform interested persons of the applicant's participation in the VFC Program and their intention of availing themselves of relief under the exemption. In Announcement 2002-31, the Service recognized that a disqualified person who met the conditions described in the proposed class exemption could, nevertheless, be subject to the sanctions of IRC section 4975 while the proposed class exemption was pending. This would be the case even though the proposed class exemption, when finalized, would cause those sanctions not to apply from the date designated by the DOL as the effective date.

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Announcement 2002-31-proposed class exemption, Continued

No excise taxes if all requirements of proposed exemption were met

In order remove a significant disincentive from participating in the VFC program, the Service stated it would not impose IRC Section 4975 (a) and (b) excise taxes if all of the requirements of the proposed class exemption were met, notwithstanding any subsequent changes to the proposed class exemption when finalized.

Certain Prohibited transactions do not fall within the exemption

Prohibited transactions under IRC Section 4975(c)(1)(F) do not fall within the framework of the DOL's proposed class exemption or Announcement 2002-31. Thus, the direct or indirect receipt of any consideration for his or her own personal account by any disqualified person who is a fiduciary from any party dealing with the plan in connection with a transaction involving the income or assets of the plan does not come within the framework of Announcement 2002-31, the proposed class exemption or PTE 2002-51 Prohibited Transaction Class Exemption 2002-51; Application No. D-10933 (67 FR 70623) was signed on November 11, 2002, and became effective with respect to transactions occurring on or after November 25, 2002.

Voluntary Fiduciary Correction Program-introduction and section 1

Introduction

The VFC Program allows certain persons to avoid potential Employee Retirement Income Security Act (ERISA) civil actions initiated by the Department of Labor, and the assessment of civil penalties under section 502(l) of ERISA in connection with investigation or civil action by the Department.

The VFC Program was designed to benefit workers by encouraging the voluntary and timely correction of possible fiduciary breaches of Part 4 of Title I of ERISA.

The interim VFC Program was put into put into effect 30 days after publication (March 15, 2000) in the Federal Register (65 FR 14164). The permanent VFC Program was adopted on March 28, 2002, effective as of April 29, 2002. The VFC Program is set forth in seven (7) Sections and three (3) Appendices.

Section 1. Purpose and Overview of the VFC Program

The purpose of the VFC Program is to protect the financial security of workers by encouraging identification and correction of transactions that violate Part 4 of Title I of ERISA (which sets out the responsibilities of employee benefit plan fiduciaries).

In general, section 409 of ERISA provides that a fiduciary who breaches any of the responsibilities in Part 4 of Title I shall be:

1. personally liable to make good to the plan any losses to the plan resulting from each breach, and
2. Required to restore to the plan any profits the fiduciary made through the use of the plan's assets.

In addition, section 405 of ERISA provides that a fiduciary may be liable, under certain circumstances, for a co-fiduciary's breach of his or her fiduciary responsibilities. In addition, under certain circumstances, there may be liability for knowing participation in a fiduciary breach.

In order to assist all affected persons in understanding the requirements of ERISA and meeting their legal responsibilities, the EBSA is providing the necessary guidance on what constitutes adequate correction under Title I of ERISA for the breaches described in the VFC Program.

VFC section 2, effect of VFC program

No action letter

The EBSA generally will issue to the applicant a **No Action Letter** with respect to a breach identified in the application if:

- the eligibility requirements under section 4 of the VFC are satisfied,
- a Plan Official corrects the breach, as defined in section 3 of the VFC, and
- the correction is in accordance with the requirements of sections 5, 6 and 7 of the VFC.

VFC section 2 Result of "no action letter"

As a result of the No Action Letter which it issues in a particular case, the EBSA will not initiate a civil investigation under Title I of ERISA for any transaction described in that No Action Letter, or will it assess a civil penalty under section 502(l) of ERISA on the correction amount paid to the plan or its participants.

Can conduct an investigation under VFC program

The EBSA reserves the right under the VFC Program to conduct an investigation at any time to determine:

1. the truthfulness and completeness of the factual statements set forth in the application, and
2. that the corrective action was, in fact, taken.

For example, any No Action Letter issued under the VFC Program is limited to the breach and persons identified in the particular application. The method of calculating the correction amount described in the VFC Program is only intended to correct the specific breach described in the application. Other methods of calculating losses may be more appropriate, depending on the facts and circumstances.

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VFC section 2, effect of VFC program, Continued

Other assumptions of VFC program

- The VFC Program assumes that the transaction (except for the designated fiduciary breach(es)) is an appropriate investment decision for the plan. Therefore, if a transaction that gives rise to violations is not addressed in the Program, such as imprudence or a failure to diversify plan assets, the relief afforded by the Program will not extend to those additional violations.

- A No Action Letter **does not imply** DOL approval of matters not included therein, including the steps that the fiduciaries may take to prevent recurrence of the breach described in the application and to ensure the plan's future compliance with Title I of ERISA.

- Any No Action Letter issued under the VFC Program **is conditioned on the truthfulness, completeness and accuracy of the statements** made in the application and of any subsequent oral and written statements or submissions. Any material misrepresentations or omissions will void the No Action Letter, retroactive to the date that the letter was issued by EBSA, with respect to the transaction that was materially misrepresented.

VFC Section 2. If application fails to satisfy terms of VFC program

If an application fails to satisfy the terms of the VFC Program, the EBSA reserves the right to investigate and take any other action with respect to the transaction and/or plan that is the subject of the application, including refusing to issue a No Action Letter.

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VFC section 2, effect of VFC program, Continued

Compliance with terms will not preclude other actions

Compliance with the terms of the VFC Program will not preclude:

1. the EBSA or any other governmental agency from conducting a criminal investigation of the transaction identified in the application;

2. the EBSA's assistance to such other agency; or

3. The EBSA from making the appropriate referrals of criminal violations as required by section 506(b) of ERISA.

In addition, compliance with the terms of the VFC Program will not preclude EBSA from taking any of the following actions:

1. Seeking removal from positions of responsibility with respect to a plan or other non-monetary injunctive relief against any person responsible for the transaction at issue;

2. Referring information regarding the transaction to the IRS as required by section 3003(c) of ERISA;

3. Imposing civil penalties under section 502(c)(2) of ERISA based on the failure or refusal to file a timely, complete and accurate annual report Form 5500.

[Note: An amended annual report filing might be required if possible breaches of ERISA have been identified, or if action is taken to correct possible breaches in accordance with the VFC Program.]
Generally, the issuance of a No Action Letter does not affect the ability of any other government agency, or any other person, to enforce any rights or carry out any authority they may have, with respect to matters described in the No Action Letter.

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VFC section 2, effect of VFC program, Continued

Example

A plan fiduciary causes the plan to purchase real estate from the plan sponsor under circumstances to which no prohibited transaction exemption applies. In connection with this transaction, the purchase causes the plan assets to no longer be diversified, in violation of ERISA section 404(a)(1)(C).

If the application reflects full compliance with the requirements of the VFC Program, the DOL's No Action Letter would apply to the prohibited transaction under ERISA section 406(a)(1)(A), but would not apply to the diversification violation under section 404(a)(1)(C).

Correction criteria

The correction criteria listed in the VFC Program represent EBSA enforcement policy and are provided for informational purposes to the public. They are not intended to confer enforceable rights on any person who purports to correct a violation.

Applicants are advised that the term "correction" as used in the VFC Program is not necessarily the same as "correction" under section 4975 of the Code.

> Please note that in footnote 7 of the final VFC Program, it is stated that the Service has indicated that except in those instances where the fiduciary breach or its correction result in a tax abuse situation or a plan qualification failure, correction under the VFC Program generally will be acceptable under the Code.

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VFC section 2, effect of VFC program, Continued

Other actions taken by the EBSA

- The EBSA reserves the right to conduct an investigation and take any other enforcement action relating to the transaction identified in a VFC Program application. These include, in certain circumstances, prejudice to the DOL that may be caused by the expiration of the statute of limitations period, material misrepresentations, or significant harm to the plan or its participants that is not cured by the correction provided under the VFC Program.

- The EBSA may also conduct a civil investigation and take any other enforcement action relating to matters not covered by the VFC Program application, or relating to other plans sponsored by the same plan sponsor, while a VFC Program application involving the plan or the plan sponsor is pending.

- The EBSA will maintain the confidentiality of any documents submitted under the VFC Program, to the extent permitted by law. However, as noted in section 2(c)(5) and (6) of the VFC Program, the EBSA has an obligation to make referrals to the IRS and to refer to other agencies evidence of criminality and other information for law enforcement purposes.

VFC program-section 3, definitions

VF C Program Section 3. Definitions

Generally, unless separately defined in the VFC Program, the terms used in the Program have the same meaning as provided in section 3 of ERISA, 29 USC section 1002.

The following definitions apply for purposes of the VFC Program:

1. **Breach:** The term "Breach" means any transaction, which is or may be a breach of the fiduciary responsibilities, contained in Part 4 of Title I of ERISA.

2. **Plan Official:** The term "Plan Official" means a plan fiduciary, plan sponsor, party in interest with respect to a plan, or other person who is in a position to correct a Breach.

3. **Under Investigation:** The term "Under Investigation" means a plan or person that is being investigated pursuant to ERISA section 504(a) or any criminal statute affecting a transaction which involves an employee benefit plan. A plan that is Under Investigation by the EBSA includes any plan for which a Plan Official, or a representative, has received oral or written notification from the EBSA of an investigation of the plan. A plan is not considered to be Under Investigation by the EBSA merely because the EBSA staff have contacted a Plan Official or representative in connection with a complaint, unless the complaint concerns the transaction described in the application.

VFC, section 4, program eligibility

VFC Program Section 4. VFC Program Eligibility

To be eligible for the VFC Program:

(a) Neither the plan nor the applicant can be Under Investigation.

(b) The application cannot contain any evidence of potential criminal violations as determined by EBSA.

VFC program, section 5, general rules for acceptable correction

Section 5(a)-Fair Market Value Determination

Many corrections require that the current or fair market value of an asset be determined as of a particular date, usually either the date the plan originally acquired the asset or the date of the correction, or both.

In order to be acceptable as part of a VFC Program correction, the valuation must meet the following conditions:

(1) Where there is a generally recognized market for the property (e.g., the New York Stock Exchange), the fair market value of the asset is the average value of the asset on that market on the applicable date. The exception to this rule is where the plan document specifies another objectively determined value such as the closing price).
(2) Where there is no generally recognized market for the asset, the fair market value of that asset must be determined in accordance with generally accepted appraisal standards by a qualified, independent appraiser and reflected in a written appraisal report signed by the appraiser.

Qualified, independent appraiser defined

An appraiser is "**qualified**" if he or she has met the education, experience, and licensing requirements that are generally recognized for appraisal of the type of asset being appraised.

An appraiser is "**independent**" only if he or she is not one of the following, does not own or control any of the following, and is not owned or controlled by, or affiliated with, any of the following:

1. The prior owner of the asset, if the asset was purchased by the plan;
2. The purchaser of the asset if the asset was or is now being sold by the plan;
3. Any other owner of the asset, if the plan is not the sole owner;
4. A fiduciary of the plan;
5. A party in interest with respect to the plan (except to the extent the appraiser becomes a party in interest when retained to perform this appraisal for the plan); or
6. The VFC Program applicant.

VFC program, section 5(b), correction amount

Introduction

Many of the transactions described in the VFC Program result in a loss to the plan or a profit to some party to the transaction. Determining the amount of the loss to the plan requires calculating how much money the plan would have now if a particular transaction had not occurred.

The VFC Program requires the fiduciary or other Plan Official to restore to the employee benefit plan the Principal Amount, plus the greater of:

1. Lost Earnings from the Loss Date to the Recovery Date or

2. Restoration of Profits resulting from the use of the Principal Amount for the same period.

The terms “Principal Amount,” “Lost Earnings,” “Loss Date,” “Recovery Date,” and “Restoration of Profits” are defined in section 5 of the VFC Program.

Definition-principal amount

The Principal Amount is the amount that would have been available to the plan for investment or distribution on the date of the Breach, had the Breach not occurred. What constitutes the Principal Amount is identified for each transaction set forth in section 7 of the VFC Program. The generic term Principal Amount is the base on which Lost Earnings are calculated.

Definition-loss date

The Loss Date is the date that the plan lost the use of the Principal Amount and the Recovery Date is the date that the Principal Amount is restored to the plan.

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VFC program, section 5(b), correction amount, Continued

Lost Earnings to be restored to the plan

For purposes of the VFC Program, Lost Earnings to be restored to a plan is the greater of:

1. The amount that otherwise would have been earned on the Principal Amount from the Loss Date to the Recovery Date had the Principal Amount been invested during the applicable period in accordance with appropriate plan provisions and Title I of ERISA, less actual net earnings or realized net appreciation (or, if applicable, plus any net loss to the plan as a result of the transaction), or

2. The amount that would have been earned on the Principal Amount at an interest rate equal to the underpayment rate defined in section 6621(a)(2) of the Code, less actual net earnings or realized net appreciation (or, if applicable, plus any net loss to the plan as a result of the transaction).

Additional amount for lost earnings if payment made after Recovery date

In addition, if the date on which the Lost Earnings is paid to the plan is a date after the Recovery Date, payment must include an additional amount that is the greater of:

1. The amount that would have been earned by the plan on the Lost Earnings if it had been paid on the Recovery Date, or

2. The amount that would have been earned on the Lost Earnings at an interest rate equal to the underpayment rate defined in section 6621(a)(2) of the Code.

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VFC program, section 5(b), correction amount, Continued

Determining lost earnings

For a participant-directed defined contribution plan, the Lost Earnings to be restored to the plan is the amount that each participant would have earned on the Principal Amount from the Loss Date to the Recovery Date.

However, for administrative convenience, the Lost Earnings amount for a participant-directed defined contribution plan may be calculated using the rate of return of the investment alternative that earned the highest rate of return among the designated broad range of investment alternatives available under the plan during the applicable period.

For a participant who has not made any participant directions, an average weighted return may be used.

Restoration of profits

The Restoration of Profits is the amount of profit made on the use of the Principal Amount, or the property purchased with the Principal Amount, by the fiduciary or party in interest who engaged in the Breach, or by a knowing participant in the Breach.

Other correction principles

- If the Principal Amount was used for a specific purpose so that the actual profit can be determined, that actual profit must be calculated from the Loss Date to the Recovery Date and returned to the plan.
- If the Principal Amount was commingled with other funds so that the actual profit cannot be determined, the Restoration of Profits will be calculated as interest on the Principal Amount at an interest rate equal to the underpayment rate defined in section 6621(a)(2) of the Code.
- In addition, if the date on which the Restoration of Profits is paid to the plan is a date after the Recovery Date, payment must include an additional amount that is the greater of:

    1. The amount that would have been earned by the plan on the Restoration of Profits if it had been paid on the Recovery Date, or
    2. The amount that would have been earned on the Restoration of Profits at an interest rate equal to the underpayment rate defined in section 6621(a)(2) of the Code.

Examples for acceptable correction under section 5

Example 1-facts

An employer who sponsors a plan with a qualified cash or deferred arrangement within the meaning of section 401(k)(2) of the Code ("401(k) plan") normally deposits participant contributions in the plan's trust account within two business days of each pay day. For this employer, the second business day after pay day is the date on which the participant contributions become plan assets, because it is the earliest date on which this employer can reasonably segregate the participant contributions from the employer's general assets. However, for the pay period ending January 31, a Monday, participant contributions totaling $10,000 were not deposited until March 2.

Example 1-determining principal amount

The Principal Amount is $10,000. The Loss Date is February 2, the date on which the participant contributions became plan assets and should have been deposited in the plan's trust account. The Recovery Date is March 2, the date that the participant contributions were deposited in the plan's trust account.

Example 1 Determining investment earnings

The 401(k) plan offers five investment alternatives that vary widely. During the month of February, one of the plan's mutual funds had a 12% annualized yield, including all reinvestment earnings. This was the highest return earned by any of the five investment alternatives in this period.

The employer elects to use this rate of return for the loss calculations. Accordingly, the Lost Earnings amount is $100 ($10,000 times 12% of the annualized yield times one-twelfth of a year).

The employer had the use of $10,000 of the 401(k) plan's assets between February 2 and March 2, while the participant contributions remained commingled with the employer's general assets. The employer's cost of funds (the actual profit from the use of the participant contributions) cannot readily be determined; therefore, the Restoration of Profits amount is calculated using the underpayment rate defined in Code section 6621(a)(2). Assuming the section 6621 rate was 9%, the Restoration of Profits amount is $75 ($10,000 times 9% per annum times one-twelfth of a year).

In this example, the Lost Earnings amount ($100) is greater than the Restoration of Profits amount ($75). Since the Principal Amount of $10,000 was paid to the plan on March 2, the total correction amount to be paid to the plan is the Lost Earnings of $100.

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Examples for acceptable correction under section 5, Continued

Example 1 Amount of correction amount if paid to plan on March 2

If the Principal Amount of $10,000 was paid to the plan on March 2, and the Lost Earnings of $100 were not paid to the plan until a year later, an additional $12 ($100 times 12 percent-the plan's annual yield), must be paid to the Plan along with the $100 Lost Earnings amount.

Example 2

On March 15, a plan's trustees authorized the purchase of 1,000 shares of stock. The plan paid $75 per share when the fair market value was $70 per share. The Principal Amount is $5,000 (1,000 shares times the $5 per share overpayment). The Loss Date is March 15, the date of the overpayment. The Recovery Date will be the date on which the fiduciary or other person repays to the plan the correction amount.

Assume that the plan recoups the $5,000 overpayment a year after the original purchase. During this year, the plan's other investments earned 9%, including all reinvestment earnings. The Lost Earnings amount is $450 ($5,000 times 9% annual yield times one year). If the Restoration of Profit amount is less than $450, the total amount to be paid to the plan is $5,450 (the Principal Amount of $5,000 plus Lost Earnings of $450).

Example 3

If the facts are the same as in Example 2 above, except that the proceeds of the sale were used to make another investment which yielded a 15% annual rate of return, the Restoration of Profits amount is $750 ($5,000 times 15% per annum times one year). In this example, the Restoration of Profits amount ($750) is greater than the Lost Earnings amount ($450). The total amount to be paid to the plan is $5,750 (the Principal Amount of $5,000 plus Restoration of Profits of $750).

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Examples for acceptable correction under section 5, Continued

Example 4

On April 20, a plan paid $6,000 in legal fees for legal services that the plan sponsor, not the plan, was obligated to pay. The Principal Amount is $6,000.

The **Loss Date** is April 20, the date the plan improperly paid the plan sponsor's legal expenses.

The **Recovery Date** will be the date on which the plan sponsor reimburses the plan $6,000. Assume that the plan sponsor reimburses the plan on October 20, six months after the Loss Date. During this period, the plan's investments earned 10% per annum, including all reinvestment earnings. **The Lost Earnings** amount is $300 ($6,000 times 10% annual yield multiplied by one-half).

In this case, the plan sponsor had constructive use of $6,000 from April 20 until October 20. The plan sponsor's cost of funds (the actual profit from the use of the money) cannot readily be determined; therefore, the Restoration of Profits amount is calculated using the underpayment rate defined in Code section 6621(a)(2). Assuming the section 6621 rate was 8% per annum, the Restoration of Profits amount is $240 ($6,000 times 8% per annum multiplied by one-half).

In this example, the Lost Earnings amount ($300) is greater than the Restoration of Profits amount ($240). As a result, the total amount to be paid to the plan is $6,300 (the Principal Amount of $6,000 plus Lost Earnings of $300).

Cost of correction, section 5(c)

Introduction

Under the DOL's rules the fiduciary, plan sponsor or other Plan Official, not the plan, must pay the costs of correction.

The principle of "Cost of Correction" is illustrated in the following example:

Example of cost of correction

The plan fiduciaries did not obtain a required independent appraisal in connection with a transaction described in Section 7 of the VFC Program. In connection with correcting the transaction, the plan fiduciaries now propose to have the appraisal performed as of the date of purchase. The plan document permits the plan to pay reasonable and necessary expenses; the fiduciaries have objectively determined that the cost of the proposed appraisal is reasonable and is not more expensive than the cost of an appraisal contemporaneous with the purchase. The plan may therefore pay for this appraisal. However, the plan may not pay any costs associated with recalculating participant account balances to take into account the new valuation.

The rationale for this correction is that there would be no need for the additional calculations or any increased appraisal cost if the plan's assets had been valued properly at the time of the purchase. Therefore, the cost of recalculating the plan participants' account balances is not a reasonable plan expense, but is part of the Costs of Correction.

VFC Program, section 5(d), Acceptable corrections, distributions

Distributions made when original distributions too low

Some plans will have to make supplemental distributions to former employees, beneficiaries receiving benefits, or alternate payees, if the original distributions were too low because of the Breach. In these situations, the Plan Official or plan administrator must determine who received distributions from the plan during the time period affected by the Breach, recalculate the account balances, and determine the amount of the underpayment to each affected individual. The applicant must demonstrate proof of payment to participants and beneficiaries whose current location is known to the plan and/or applicant.

For individuals whose location is unknown to the plan and/or applicant, applicants must demonstrate that they have segregated adequate funds to pay the missing individuals and that the applicant has commenced the process of locating the missing individuals using either the IRS and Social Security Administration locator services, or other comparable means. The costs of these efforts are part of the Costs of Correction.

VFC program, section 5(e), de-minimus exception

De Minimus Exception-5(e)

Where correction under the VFC Program requires distributions in amounts:

- less than $20 to former employees, their beneficiaries and alternate payees, who neither have account balances with, nor have a right to future benefits from the plan, and
- the applicant demonstrates in its submission that the cost of making these distributions exceeds the amount of the payment to which an individual is entitled in connection with the correction of the transaction that is the subject of the application,

the applicant need not make distributions to those individuals who would receive less than $20 each as part of the correction. However, the applicant **must pay to the plan** the total de minimus amounts that are not distributed to such individuals.

Example of de-minimus

Employer X sponsors Plan Y. Employer X submits an application under the VFC Program to correct a failure to forward timely participant contributions to Plan Y. Employer X paid the delinquent contributions six months late, but did not pay the lost earnings on the delinquency. The correction under the VFC Program, therefore, required only payment of Lost Earnings for the six-month delinquency.

During the six-month period 25 employees separated from service and rolled over their plan accounts to individual retirement accounts. The amount of lost earnings due to 20 of those former employees is less than $20, and Employer X demonstrates that the cost of making the distribution to those former employees is $27 per individual.

Employer X need not make distributions to those 20 former employees. However, the total amount of distributions that would have been due to those former employees must be paid to Plan Y. The payment to Plan Y may be used for any purpose that payments or credits to Plan Y that are not allocated directly to participant accounts are used.

Under this *de minimus* exception, Employer X must make distributions to the five former employees who are entitled to receive distributions of more than $20

VFC program, section 6, application procedures

VFC Program Section 6. Application Procedures

Section 6 of the VFC Program pertains to application procedures that must be followed in order to obtain a No Action letter from EBSA. For details on the application process, see section 6 of Exhibit 3 as supplemented for specific corrections described below.

VFC Program, section 7, eligible transactions

Introduction

EBSA has identified those Breaches and methods of correction that it believes are suitable for the VFC Program. Any Plan Official may correct a Breach listed in Section 7 of the VFC Program in accordance with the applicable correction method.

The correction methods set forth are strictly construed and are the only acceptable correction methods under the VFC Program for the transactions described in Section 7. EBSA will not accept applications concerning correction of breaches not described in Section 7.

Announcement 2002-31, which was effective between March 28, 2002, and November 24, 2002, and PTE 2002-51, which became effective November 25, 2002, grant excise tax relief for some of the breaches in the VFC Program. The rationale for granting limited excise tax relief is set forth extensively in the March 28, 2002, preamble to the proposed class exemption and to a lesser extent in the preamble to the final VFC Program and in Announcement 2002-31.

VFC program, section 7A-eligible transactions and corrections

Eligible transaction-delay in making contributions

An employer receives directly from participants, or withholds from employees' paychecks, certain amounts for contribution to a pension plan. Instead of forwarding the contributions for investment in accordance with the provisions of the plan and within the time frames described in the DOL's regulations (29 CFR 2510.3-102), the employer retains the contributions for a longer period of time.

Correction for unpaid contributions

For participant contributions not yet paid to the plan, correction will consist of paying to the plan the Principal Amount, plus the greater of:

(i) Lost Earnings on that Principal Amount or

(ii) Restoration of Profits resulting from the employer's use of the Principal Amount.

The Principal Amount is the amount of the unpaid participant contributions. The Loss Date for each participant contribution is the earliest date on which it could reasonably have been segregated from the employer's general assets. In no event shall the Loss Date be later than the applicable maximum time period described in section 2510.3-102 of the DOL’s regulations.

Correction of Late contributions

If the participant contributions were remitted to the plan outside the time period required by the aforementioned regulation, the only correction required is to pay to the plan the greater of:

(i) Lost Earnings or
(ii) Restoration of Profits resulting from the employer's use of the Principal Amount

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Section 7(a)-Examples illustrating delay of contributions and correction

Example 1 illustrating transaction and correction

An employer who sponsors a plan with a qualified cash or deferred arrangement within the meaning of section 401(k)(2) of the Code ("401(k) plan") normally deposits participant contributions in the plan's trust account within two business days of each pay day. For this employer, the second business day after pay day is the date on which the participant contributions become plan assets, because it is the earliest date on which this employer can reasonably segregate the participant contributions from the employer's general assets. However, for the pay period ending January 31, a Monday, participant contributions totaling $10,000 were not deposited until March 2.

Example1 Determining principal amount, loss date, recovery date

The **Principal Amount** is $10,000. The **Loss Date** is February 2, the date on which the participant contributions became plan assets and should have been deposited in the plan's trust account. The **Recovery Date** is March 2, the date that the participant contributions were deposited in the plan's trust account.

Example 1 Determining lost earnings and restoration of profits

The 401(k) plan offers five widely varying investment alternatives. During the month of February, one of the plan's mutual funds had a 12% annualized yield, including all reinvestment earnings. This was the highest return earned by any of the five investment alternatives in this period. The employer elects to use this rate of return for the loss calculations. **Accordingly, the Lost Earnings amount is $100 ($10,000 times 12% annualized yield times one-twelfth of a year)**.

Example 1 Determining restoration of profits

The employer had the use of $10,000 of the 401(k) plan's assets between February 2 and March 2, while the participant contributions remained commingled with the employer's general assets. The employer's cost of funds (the actual profit from the use of the participant contributions) cannot readily be determined; therefore, the Restoration of Profits amount is calculated using the underpayment rate defined in Code section 6621(a)(2). Assuming the section 6621 rate was 9%, **the Restoration of Profits amount is $75** ($10,000 times 9% per annum times one-twelfth of a year).

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Section 7(a)-Examples illustrating delay of contributions and correction, Continued

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Example 1 Determining the correction for lost earnings

In this example, the Lost Earnings amount ($100) is greater than the Restoration of Profits amount ($75). Since the Principal Amount of $10,000 was paid to the plan on March 2, the total correction amount to be paid to the plan is the Lost Earnings of $ 100.

Example 1 Correction

If the Principal Amount of $10,000 was paid to the plan on March 2, and, the Lost Earnings of $100 were not paid to the plan until a year later, an additional $12 ($100 times 12 percent-the plan's annual yield), must be paid to the Plan along with the $100 Lost Earnings amount.

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Section 7(a)-Examples illustrating delay of contributions and correction, Continued

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Example 2-facts

Employer X is a large national corporation, which sponsors a section 401(k) plan. X is able to segregate participant contributions no later than 10 business days after the end of the month in which participant contributions were withheld from employees' paychecks. For the pay period ending June 15, participant contributions totaling $ 900,000 were not deposited until August 14.

Example 2 Principal amount, loss date etc.

The **Principal Amount is $900,000**. The **Loss Date** is July 14 (the tenth business day in July), the date on which the participant contributions became plan assets and should have been deposited in the plan's trust account. **The Recovery Date is August 14**, the date that the participant contributions were deposited in the plan's trust account.

Example 2 Determining earnings correction

The 401(k) plan offers eight widely varying investment alternatives with daily asset valuation. From July 14 through August 14, most of the plan participants experienced a decline in their account balances due to a decline in the stock market; however, some participants had a net investment gain. The Code section 6621(a)(2) rate during this period was 8% and was greater than the profit to the employer from the use of the funds during the pertinent time period.

For the participants whose account balances declined, the employer pays the Principal Amount plus the Restoration of Profits amount, calculated at 8%. For the other participants, the employer pays the Principal Amount plus the higher of each participant's actual investment earnings between July 14 and August 14 or the Restoration of Profits amount calculated at 8%.

Example 2 Correction

Since the Principal Amount of $900,000 has already been paid to the plan, the correction amount to be paid to the plan is no less than the Restoration of Profits of $6,000 ($900,000 times 8% per annum times one-twelfth of a year).

Example 2 Additional documentation

In addition to the documentation required in section 6 of the VFC Program, the Applicant must also submit the additional material described in section 7.A.1 of Exhibit 3.

VFC program, section 7.B.2-loans at fair market value interest rate to parties in interest

Loans at fair market value-7.B.1-eligible transaction

A plan made a loan to a party in interest at an interest rate no less than that for loans with similar terms (for example, the amount of the loan, amount and type of security, repayment schedule, and duration of loan) to a borrower of similar creditworthiness. The loan was not exempt from the prohibited transaction provisions of Title I of ERISA.

Correction under VFC program

The loan must be paid in full, including any prepayment penalties. In addition, an independent commercial lender must also confirm in writing that the loan was made at a fair market interest rate for a loan with similar terms to a borrower of similar creditworthiness.

Additional documentation

In addition to the documentation required by Section 6 of the VFC Program, the applicant must submit a narrative describing the process used to determine the fair market interest rate at the time the loan was made, validated in writing by an independent commercial lender.

Loans at below market interest rate to parties in interest-section 7.B.2

Loans at below market interest rate-eligible transaction

A plan made a loan to a party in interest with respect to the plan at an interest rate which, at the time the loan was made, was less than the fair market interest rate for loans with similar terms (for example, the amount of loan, amount and type of security, repayment schedule, and duration of the loan) to a borrower of similar creditworthiness. The loan was not exempt from the prohibited transaction provisions of Title I of ERISA.

Correction of transaction

The loan must be paid in full, including any prepayment penalties. The party in interest or Plan Official must pay to the plan the Principal Amount, plus the greater of:

a. the Lost Earnings, or

b. the Restoration of Profits, if any, as previously described above.

For these purposes, the Principal Amount is equal to the excess of the interest payments that would have been received if the loan had been made at the fair market interest rate (from the beginning of the loan until the Recovery Date) over the interest payments actually received under the loan terms during the period.

For purposes of the VFC Program, an independent commercial lender must determine the fair market interest rate. The Plan must pay any supplemental distributions that are due as a result of the increase.

Example illustrating below market value interest rate

The plan made a $150,000 mortgage loan to a party in interest, secured by a first Deed of Trust, at a fixed interest rate of 4% per annum. The loan was to be fully amortized over 30 years. The fair market interest rate for comparable loans, at the time this loan was made, was 7% per annum. The party in interest or Plan Official must repay the loan in full plus any applicable prepayment penalties.

The party in interest or Plan Official also must pay the difference between what the plan would have received through the Recovery Date had the loan been made at 7% and what, in fact, the plan did receive from the commencement of the loan to the Recovery Date, plus lost earnings on that amount.

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Loans at below market interest rate to parties in interest-section 7.B.2, Continued

Additional documentation required

In addition to the documentation required in section 6 of the VFC Program, the Applicant must also submit the documentation described in section 7.B.1 of Exhibit 3

VFC program-loan at below market interest to a non-party in interest

Eligible transaction

A plan made a loan to a person who is not a party in interest with respect to the plan at an interest rate which, at the time the loan was made, was less than the fair market interest rate for loans with similar terms (for example, the amount of loan, amount and type of security, repayment schedule, and duration of the loan) to a borrower of similar creditworthiness.

Correction of transaction

The borrower or Plan Official must pay to the plan the Principal Amount, plus Lost Earnings through the Recovery Date.

Each loan payment has a Principal Amount equal to the excess of:

(a) the interest payments that would have been received until the Recovery Date if the loan had been made at the fair market interest rate, over

(b) the interest actually received under the loan terms.

An independent commercial lender must determine the fair market interest rate. From the inception of the loan to the Recovery Date, the amount to be paid to the plan is the Lost Earnings on the series of Principal Amounts.

From the Recovery Date to the maturity date of the loan, the amount to be paid to the plan is the present value of the remaining Principal Amounts, as determined by an independent commercial lender. Instead of calculating the present value, it is acceptable for administrative convenience to pay the sum of the remaining Principal Amounts.

Continued on next page

VFC program-loan at below market interest to a non-party in interest, Continued

Example

The plan made a $ 150,000 mortgage loan, secured by a first Deed of Trust, at a fixed interest rate of 4% per annum. The loan was to be fully amortized over 30 years. The fair market interest rate for comparable loans, at the time this loan was made, was 7% per annum.

The borrower or the Plan Official must pay the excess of what the Plan would have received through the Recovery Date had the loan been made at 7% over what, in fact, the plan did receive from the commencement of the loan to the Recovery Date, plus Lost Earnings on that amount. The Plan Official must also pay on the Recovery Date the difference in the value of the remaining payments on the loan between the 7% and the 4% for the duration of the time the plan is owed repayments on the loan.

Additional documentation required

In addition to the documentation already required in section 6 of the VFC Program, the Applicant must also submit the additional documentation described in section 7.B.3 of Exhibit 3.

Loan at below market interest rate solely due to delay in perfecting plan's security interest, VFC program, 7.B.4

Eligible transaction

A plan made a purportedly secured loan to a person who is not a party in interest with respect to the plan, and there was a delay in recording or otherwise perfecting the plan's interest in the loan collateral. The loan will be treated as an unsecured loan until the plan's security interest was perfected.

Correction of transaction

The borrower or the Plan Official must pay to the plan the Principal Amount, plus Lost Earnings through the date the loan is fully secured.

The Principal Amount is equal to the difference between:

(a) interest payments actually received under the loan terms and

(b) the interest payments that would have been received if the loan had been made at the fair market interest rate for an unsecured loan.

An independent commercial lender must determine the fair market interest rate.

If the delay in perfecting the loan's security caused a permanent change in the risk characteristics of the loan, an independent commercial lender must determine the fair market interest rate for the remaining term of the loan.

In that case the correction amount includes an additional amount equal to the present value of the remaining Principal Amounts from the date the loan is fully secured to the maturity date of the loan to must be paid to the plan. Instead of calculating the present value, it is acceptable for administrative convenience to pay the sum of the remaining Principal Amounts.

Example

The plan made a mortgage loan, which was supposed to be secured by a Deed of Trust. The plan's Deed was not recorded for six months, but, when it was recorded, the Deed was in first position. The interest rate on the loan was the fair market interest rate for a mortgage loan secured by a first-position Deed of Trust. The loan is treated as an unsecured, below-market loan for the six months prior to the recording of the Deed of Trust.

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Loan at below market interest rate solely due to delay in perfecting plan's security interest, VFC program, 7.B.4,
Continued

Example	If the same facts are used as in the above example except that, as a result of the delay in recording the Deed, the plan ended up in second position behind another lender. The risk to the plan is higher and the interest rate on the note is no longer commensurate with that risk. The loan is treated as a below-market loan (based on the lack of security) for the six months prior to the recording of the Deed of Trust and as a below-market loan (based on secondary status security) from the time the Deed is recorded until the end of the loan.
Additional documentation required	In addition to the documentation already required in section 6 of the VFC Program, the Applicant must also submit the additional documentation described in section 7.B.4 of Exhibit 3.

Purchase of asset (including real property) by a plan from a party in interest

Eligible transaction

A plan purchased an asset with cash from a party in interest with respect to the plan, and under the circumstances; no prohibited transaction exemption applies.

Correction of transaction

The transaction must be corrected by the sale of the property back to the party in interest who originally sold the asset to the plan or to a person who is not a party in interest. Whether the asset is sold to a person who is not a party in interest with respect to the plan or is sold back to the original seller, the plan must receive the higher of:

1. the fair market value (FMV) of the asset at the time of resale, without a reduction for the costs of sale; or

2. the Principal Amount, plus the greater of:
   a. the Lost Earnings on the Principal Amount, or
   b. the Restoration of Profits.

For this transaction, the Principal Amount is the plan's original purchase price.

Example

A plan purchased from the plan sponsor a parcel of real property. The plan does not lease the property to any person. Instead, the plan uses the property as an office. The Plan Official obtains from a qualified, independent appraiser an appraisal of the property reflecting the FMV of the property at the time of purchase. The appraiser values the property at $100,000, although the plan paid the plan sponsor $120,000 for the property. As of the Recovery Date the property is valued at $110,000.

To correct the transaction, the plan sponsor repurchases the property for $120,000 with no reduction for the costs of the sale and reimburses the plan for the initial costs of the sale. In addition, the plan sponsor also must pay the plan the greater of the plan's Lost Earnings or the sponsor's profits on this amount. This example assumes that the plan sponsor did not make a profit on the $120,000 proceeds from the original sale of the property to the plan.

Continued on next page

Purchase of asset (including real property) by a plan from a party in interest, Continued

Additional documentation required

In addition to the documentation already required in section 6 of the VFC Program, the Applicant must also submit the additional documentation described in section 7.C.1 of Exhibit 3.

Sale of an Asset (Including Real Property) by a Plan to a Party in Interest (VFC Program Section 7.C.2)

Eligible transaction

A plan sold an asset for cash to a party in interest with respect to the plan, in a transaction that is not exempt from the prohibited transaction provisions of Title I of ERISA.

Correction

The plan must receive the Principal Amount plus the greater of:

1. the Lost Earnings, or

2. the Restoration of Profits, if any.

Continued on next page

Sale of an Asset (Including Real Property) by a Plan to a Party in Interest (VFC Program Section 7.C.2), Continued

Alternative to repayment

As an alternative to repayment of the Principal Amount, if it is determined that the plan will realize a greater benefit by repurchasing the property, the plan may repurchase the asset from the party in interest at the lower of the price for which it sold the property or the FMV of the property as of the Recovery Date plus restoration of the party in interest's net profits from owning the property, to the extent they exceed the plan's investment return from the proceeds of the sale.

The determination as to which correction alternative the plan chooses must be made by an independent fiduciary. The repurchase of the same property from the party in interest to whom the asset was sold is a reversal of the original prohibited transaction. This sale is not a new prohibited transaction and therefore does not require an exemption.

For this transaction, the Principal Amount is the amount by which the FMV of the asset (at the time of the original sale) exceeds the sale price.

Example

A plan sold a parcel of unimproved real property to the plan sponsor. The sponsor did not make any profit on the use of the property. The Plan Official obtains from a qualified, independent appraiser an appraisal of the property reflecting the FMV of the property as of the date of sale. The appraiser valued the property at $130,000, although the plan sold the property to the plan sponsor for $120,000. However, the plan fiduciaries have reason to believe that the property will substantially increase in the near future based on the anticipated building of a shopping mall adjacent to the property in question and, as of the Recovery Date, the appraiser values the property at $140,000.

An independent fiduciary determines that the property is a prudent investment for the plan, and will not result in any liquidity or diversification problems. The plan corrects by repurchasing the property at the original sale price, with the party in interest assuming the costs of the reversal of the sale transaction.

Additional documentation required

In addition to the documentation already required in section 6 of the VFC Program, the Applicant must also submit the additional documentation described in section 7.C.2 of Exhibit 3.

Sale and Leaseback of Real Property to Employer (VFC Program Section 7.C.3)

Eligible transaction

The plan sponsor sold a parcel of real property to the plan, which then was leased back to the sponsor, in a transaction that is not otherwise exempt.

Correction of transaction

The transaction must be corrected by the sale of the parcel of real property back to the plan sponsor or to a person who is not a party in interest with respect to the plan.

The plan must receive the higher of

1. the FMV of the asset at the time of resale, without a reduction for the costs of sale; or

2. the Principal Amount, plus the greater of:
   a. the Lost Earnings on the Principal Amount or
   b. the Restoration of Profits, if any.

If the plan purchased the property from the plan sponsor, the sale of the same property back to the plan sponsor is a reversal of the prohibited transaction. The sale is not a new prohibited transaction and therefore does not require an individual prohibited transaction exemption, as long as the plan did not make improvements while it owned the property.

If the plan was not receiving rent

If the plan has not been receiving rent at FMV, as determined by a qualified, independent appraisal, the sale price of the real property should not be based on the historic below-market rent that was paid to the plan.

Continued on next page

Sale and Leaseback of Real Property to Employer (VFC Program Section 7.C.3), Continued

Additional correction amount required

In addition to the requirements for a correction described above, if the plan was not receiving rent at FMV, as determined by a qualified, independent appraiser, the Principal Amount will also include the difference between the rent actually paid and the rent that should have been paid at FMV. The plan sponsor must pay to the plan this additional Principal Amount, plus the greater of:

1. the Lost Earnings or
2. the Restoration of Profits resulting from the plan sponsor's use of the Principal Amount.

Example

The plan purchased at FMV from the plan sponsor an office building that served as the sponsor's primary business site. Simultaneously, the plan sponsor leased the building from the plan at below the market rental rate. The Plan Official obtains from a qualified, independent appraiser an appraisal of the property reflecting the FMV of the property and rent.

To correct the transaction, the plan sponsor purchases the property from the plan at the higher of the appraised value at the time of the resale or the original sales price and also pays the Lost Earnings. Because the rent paid to the plan was below the market rate, the sponsor must also make up the difference between the rent paid under the terms of the lease and the amount that should have been paid, plus Lost Earnings on this amount.

Additional documentation required

In addition to the documentation already required in section 6 of the VFC Program, the Applicant must also submit the documentation described in section 7.C.3 of Exhibit 3.

Purchase of an asset (including real property) from the plan by a non-party in interest at a price other than fair market value (VFC Program Section 7.C.4)

Eligible transaction	A plan acquired an asset from a person who is not a party in interest with respect to the plan, without determining the asset's FMV. As a result, the plan paid more than it should have for the asset.
Correction of transaction	The Principal Amount is the difference between the actual purchase price and the asset's FMV at the time of purchase. The plan must receive the Principal Amount plus the Lost Earnings.
Example	A plan bought unimproved land without obtaining a qualified, independent appraisal. Upon discovering that the purchase price was $10,000 more than the appraised FMV, the Plan Official pays the plan the Principal Amount of $10,000, plus Lost Earnings.
Additional documentation required	In addition to the documentation already required in section 6 of the VFC Program, the Applicant must also submit the additional documentation described in section 7.C.4 of Exhibit 3.

Sale of an asset (including real property) by a plan to a non-party in interest at a price less than fair market value (VFC program Section 7.C.5)

Eligible Transaction	A plan sold an asset to a person who is not a party in interest with respect to the plan, without determining the asset's FMV. As a result, the plan received less than it should have from the sale.
Correction of Transaction	The Principal Amount is the amount by which the FMV of the asset as of the Recovery Date exceeds the price at which the plan sold the property. The plan must receive the Principal Amount plus Lost Earnings.
Example	A plan sold unimproved land without taking steps to ensure that the plan received FMV. Upon discovering that the sale price was $10,000 less than the FMV, the Plan Official pays the plan the Principal Amount of $10,000 plus Lost Earnings.
Additional Documentation Required	In addition to the documentation already required in section 6 of the VFC Program, the Applicant must also submit the additional documentation described in section 7.C.5 of Exhibit 3.

Payment of benefits without properly valuing plan assets on which payment is based (VFC Program Section 7.D.1)

Eligible Transaction

A defined contribution pension plan pays benefits based on the value of the plan's assets. If one or more of the plan's assets are not valued at current value, the benefit payments are not correct. If the plan's assets are overvalued, the current benefit payments will be too high. If the plan's assets are undervalued, the current benefit payments will be too low.

Correction of Transaction

The correct value of the improperly valued asset for each plan year must be established starting with the first plan year in which the asset was improperly valued. The Plan Officials must:

1. For overvaluations, restore to the plan the excess distributions to the affected plan participants (plus the Lost Earnings as described in *Example 1* below).

2. For undervaluations, restore directly to the plan participants, the amount by which all affected participants were underpaid distributions to which they were entitled under the terms of the plan, plus the higher of Lost Earnings or the underpayment rate defined in section 6621(a)(2) of the Code on the underpaid distributions.

3. File amended Annual Report Forms 5500 as described in section 7.D.1 of Exhibit 3.

Continued on next page

Payment of benefits without properly valuing plan assets on which payment is based (VFC Program Section 7.D.1),
Continued

Correcting the valuation defect

To correct the valuation defect, a Plan Official must determine the FMV of the improperly valued asset for each year in which the asset was valued improperly. Once the FMV has been determined, the participant account balances for each year must be adjusted accordingly.

The Plan Official or plan administrator must determine who received distributions from the plan during the time the asset was valued improperly. For distributions that were too low, the amount of the underpayment is treated as a Principal Amount for each individual who received a distribution.

The Principal Amount and the Lost Earnings must be paid to the affected individuals. For distributions that were too high, the total of the overpayments constitutes the Principal Amount for the plan. The Principal Amount plus the Lost Earnings must be restored to the plan or to the participants.

Example

On December 31, 1995, a profit sharing plan purchased a 20-acre parcel of real property for $ 500,000, which represented a portion of the plan's assets. The plan carried the property on its books at cost, rather than at FMV. One participant left the company on January 1, 1997, and received a distribution, which included her portion of the value of the property. The separated participant's account balance represented 2% of the plan's assets. As part of correction for the VFC Program, a qualified, independent appraiser has determined the FMV of the property for 1996, 1997, and 1998. The FMV as of December 31, 1996, was $400,000. Therefore, this participant was overpaid by $2,000 (($500,000-$ 400,000) times 2%).

The Plan Officials corrected the transaction by paying to the plan $2,500, consisting of $2,000 Principal Amount and $500 Lost Earnings. The Lost Earnings were based on a return of 25%, which represents the total return on the plan's investments from the date of the distribution to the participant until the date of correction.

The plan administrator also filed an amended Form 5500 for plan years 1996 and 1997, to reflect the proper values. The plan administrator will include the correct asset valuation in the 1998 Form 5500 when that form is filed.

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Payment of benefits without properly valuing plan assets on which payment is based (VFC Program Section 7.D.1),

Continued

Example

If the same facts are assumed as in the above Example, except that the property had appreciated in value to $600,000 as of December 31, 1996, -the separated participant would have been underpaid by $2,000. The correction consists of locating the participant and distributing $2,500 to her ($2,000 Principal Amount and $ 500 Lost Earnings), as well as filing the amended 5500 series forms.

Additional Documentation Required

In addition to the documentation already required in section 6 of the VFC Program, the Applicant must also submit the additional documentation described in section 7.D.1 of Exhibit 3.

Duplicative, excessive, or unnecessary compensation paid by a plan (VFC Program Section 7.E.1)

Eligible transaction

Assume that a plan paid:

1. excessive compensation, including commissions or fees, to a service provider (such as an attorney, accountant, actuary, financial advisor, or insurance agent),

2. two or more persons to provide the same services to the plan, or

3. a service provider for services that were not necessary for the operation of the plan.

Correction of Transaction

The Plan Officials must restore to the plan the Principal Amount, plus the greater of:

1. the Lost Earnings or

2. the Restoration of Profits resulting from the use of the Principal Amount.

The Principal Amount is the difference between:

1. the amount actually paid by the plan to the service provider during the six years prior to the discontinuation of the payment of the excessive, duplicative, or unnecessary compensation and

2. the reasonable market value of the non-duplicative services.

Continued on next page

Duplicative, excessive, or unnecessary compensation paid by a plan (VFC Program Section 7.E.1), Continued

Example

A plan hired an investment advisor who advised the plan's trustees about how to invest the plan's entire portfolio. In accordance with the plan document, the trustees instructed the advisor to limit the plan's investments to equities and bonds. In exchange for his services, the plan paid the investment advisor 3% of the value of the portfolio's assets.

If the trustees had inquired they would have learned that comparable investment advisors charged 1% of the value of the assets for the type of portfolio that the plan maintained.

To correct the transaction, the plan must be paid the Principal Amount of 2% of the value of the plan's assets, plus Lost Earnings.

Additional Documentation Required

In addition to the documentation already required in section 6 of the VFC Program, the Applicant must also submit the additional documentation described in section 7.E.1 of Exhibit 3.

Payment of Dual Compensation to a Plan Fiduciary (VFC Program Section 7.E.2)

Eligible Transaction

A plan pays a fiduciary for services rendered to the plan when the fiduciary already receives full-time pay from an employer or an association of employers, whose employees are participants in the plan, or from an employee organization whose members are participants in the plan. The plan's payments to the plan fiduciary are not mere reimbursements of expenses properly and actually incurred by the fiduciary.

Correction of Transaction

Restoring to the plan the Principal Amount, plus the greater of:

1. the Lost Earnings or
2. the Restoration of Profits resulting from the fiduciary's use of the Principal Amount for the same period.

The Principal Amount is the difference between:

1. the amount actually paid by the plan during the six years prior to the discontinuation of the payments to the fiduciary and
2. the amount that represents reimbursements of expenses properly and actually incurred by the fiduciary.

Example

A union sponsored a health plan funded through contributions by employers. The union president receives $50,000 per year from the union in compensation for his services as union president. He is appointed as a trustee of the health plan while retaining his position as union president. In exchange for acting as plan trustee, the union president is paid a salary of $200 per week by the plan while still receiving the $50,000 salary from the union. Since $50,000 is full-time pay, the plan's weekly salary payments are improper.

To correct the transaction, the plan must be paid the Principal Amount, which is the $200 weekly amount for each week that the salary was paid, plus the higher of Lost Earnings or Restoration of Profits.

Continued on next page

Payment of Dual Compensation to a Plan Fiduciary (VFC Program Section 7.E.2), Continued

Additional documentation required

In addition to the documentation already required in section 6 of the VFC Program, the Applicant must also submit the additional material described in section 7.E.2 of Exhibit 3.

A sample DOL no action letter appears as Appendix A to Exhibit 3 and a checklist of items needed for an application appears as Appendix B to Exhibit 3. In addition, the DOL has posted answers to some of the more frequently asked questions regarding its VFC Program. These FAQs can be found at http://www.dol.gov/ebsa/faqs/faq_vfcp.html .

EXHIBIT 1 PROHIBITED TRANSACTION CLASS EXEMPTION 2002-51

DEPARTMENT OF LABOR (DOL)

Pension and Welfare Benefits Administration (PWBA)

[Prohibited Transaction Exemption 2002-51; Application No. D-10933]

Class Exemption to Permit Certain Transactions Identified in the Voluntary Fiduciary Correction Program

67 FR 70623

DATE: Monday, November 25, 2002

ACTION: Grant of class exemption.

SUMMARY: This document contains a final exemption from certain prohibited transaction restrictions of the Internal Revenue Code of 1986 (the Code). The exemption was proposed in conjunction with the Department's Voluntary Fiduciary Correction (VFC) Program, the final version of which was published in the March 28, 2002, issue of the Federal Register. The VFC Program allows certain persons to avoid potential civil actions under the Employee Retirement Income Security Act of 1974 (ERISA) initiated by the Department and the assessment of civil penalties under section 502(l) of ERISA in connection with investigation or civil action by the Department. The exemption will affect plans, participants and beneficiaries of such plans and certain other persons engaging in such transactions.

EFFECTIVE DATE: The exemption is effective November 25, 2002.

FOR FURTHER INFORMATION CONTACT: Karen E. Lloyd, Office of Exemption Determinations, Pension and Welfare Benefits Administration, U.S. Department of Labor, Room N-5649, 200 Constitution Avenue, NW., Washington, DC 20210, (202) 693-8540 (not a toll free number) or Cynthia Weglicki, Plan Benefits Security Division, Office of the Solicitor, U.S. Department of Labor, 200 Constitution Avenue, NW., Washington, DC 20210, (202) 693-5600 (not a toll free number).

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EXHIBIT 1 PROHIBITED TRANSACTION CLASS EXEMPTION 2002-51, Continued

SUPPLEMENTARY INFORMATION: On March 28, 2002, the Department published a notice in the Federal Register (67 FR 15083) of the pendency of a proposed class exemption from the sanctions resulting from the application of section 4975(a) and (b) of the Code, by reason of section 4975(c)(1)(A) through (E) of the Code. The Department proposed the class exemption on its own motion pursuant to section 4975(c)(2) of the Code, and in accordance with the procedures set forth in 29 CFR part 2570, subpart B (55 FR 32836, August 10, 1990). n1

n1 Section 102 of the Reorganization Plan No. 4 of 1978, 5 U.S.C. App. 1 (1996) generally transferred the authority of the Secretary of the Treasury to issue exemptions under section 4975(c)(2) of the Code to the Secretary of Labor.

The notice of pendency gave interested persons an opportunity to comment or request a public hearing on the proposal. Two (2) public comments were received by the Department. Upon consideration of the comments received, the Department has determined to grant the proposed class exemption subject to certain modifications. These [*70624] modifications and the comments are discussed below.

Executive Order 12866

Under Executive Order 12866, the Department must determine whether a regulatory action is "significant" and therefore subject to the requirements of the Executive Order and subject to review by the Office of Management and Budget (OMB). Under section 3(f), the order defines a "significant regulatory action" as an action that is likely to result in a rule (1) having an annual effect on the economy of $ 100 million or more, or adversely and materially affecting a sector of the economy, productivity, competition, jobs, the environment, public health or safety, or State, local or tribal governments or communities (also referred to as "economically significant"); (2) creating serious inconsistency or otherwise interfering with an action taken or planned by another agency; (3) materially altering the budgetary impacts of entitlement grants, user fees, or loan programs or the rights and obligations of recipients thereof; or (4) raising novel legal or policy issues arising out of legal mandates, the President's priorities, or the principles set forth in the Executive Order.

Pursuant to the terms of the Executive Order, it was determined that this action is "significant" under Section 3(f)(4) of the Executive Order. Accordingly, this action has been reviewed by OMB.

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EXHIBIT 1 PROHIBITED TRANSACTION CLASS EXEMPTION 2002-51, Continued

Paperwork Reduction Act

In accordance with the Paperwork Reduction Act of 1995 (44 U.S.C. 3501-3520)(PRA 95), the Department submitted the information collection request (ICR) included in the Proposed Class Exemption to Permit Certain Transactions Identified in the Voluntary Fiduciary Correction to the Office of Management and Budget (OMB) for review and clearance at the time the Notice of the Proposed Class Exemption was published in the Federal Register (March 28, 2002, 67 FR 15083). OMB approved the Notice under OMB control number 1210-0118. The approval will expire on November 30, 2003.

The Department solicited comments concerning the ICR in connection with the Notice of Proposed Class Exemption. The Department received no comments addressing its burden estimates and no substantive changes have been made in the final exemption that would affect the Department's earlier burden estimates.

Agency: Pension and Welfare Benefits Administration, Department of Labor.

Title: Voluntary Fiduciary Correction Program.

OMB Number: 1210-0118.

Affected Public: Business or other for-profit; Not-for-profit institutions.

Respondents: 700.

Frequency of Response: On occasion.

Responses: 700.

Estimated Total Burden Hours: 5,710 hours.

Total Burden Cost (Operating and Maintenance): $ 272,928.

Discussion of Comments Received

The Department received two comments regarding the proposed class exemption. The commenters requested specific modifications to the proposal in the following areas:

1. Notice to Interested Persons

Both commenters addressed Section IV of the proposed exemption which required applicants to provide notice to interested persons of the transaction and the method of correction. It was noted that, in many cases, applicants who may be subject to the excise taxes under section 4975 of the Code will not be the employer whose employees are covered by the plan, and may be unrelated to the employer.

Continued on next page

EXHIBIT 1 PROHIBITED TRANSACTION CLASS EXEMPTION 2002-51, Continued

In this regard, one of the commenters stated that, without the cooperation of the employer, applicants might find it difficult to provide notice to participants and beneficiaries because they would not have access to the participants' and beneficiaries' names and addresses. The commenter further noted that employers might not be willing to provide access to such information due to privacy concerns or concerns that receipt of the notice might cause confusion among the participants and beneficiaries.

In the commenter's view, relief under the exemption should not be conditioned on the cooperation of an employer or other person that is unrelated to the applicant, particularly since the underlying prohibited transaction will have been corrected pursuant to the VFC Program. The commenter proposed that, in the case of an applicant unrelated to the employer whose employees are covered by the plan, the exemption permit notice to be provided to the employer or other plan fiduciary unrelated to the applicant who was not involved in the transaction that is the subject of the VFC Program application, rather than each participant and beneficiary. The commenter noted that the unrelated fiduciary could then determine whether plan participants and beneficiaries should be notified of the underlying transaction and its correction under the VFC Program.

The other commenter stated generally that the notice requirement was unnecessary and burdensome, but subsequently clarified that it had the same concerns as the first commenter.

The Department concurs with the commenters' views on the notice issue. In this regard, the Department notes that the proposed exemption does not contain a definition of interested persons to whom notice must be provided. It is the view of the Department that, where an applicant is unaffiliated with, and unrelated to, the employer whose employees are covered by the plan, the notice requirement will be deemed satisfied if the applicant provides notice to a fiduciary of the plan who is unrelated to the applicant and all other parties involved in the prohibited transaction. In many cases, this may be the employer or an administrative committee composed of officers and employees of the employer. However, the Department cautions that the notice requirement will not be considered satisfied if notice is given to an employer who is not unrelated to all parties involved in the prohibited transaction. Under no circumstances should plan assets be used to pay for the notice.

2. Three Year Rule

One of the commenters also was concerned about Section II.F. of the proposed exemption, which provided that an applicant seeking relief under the exemption could not have taken advantage of the relief provided under the VFC Program and this exemption for a similar type of transaction identified in the current application during the period which is three years prior to the submission of the current application. The commenter argued that applicants that are service providers, as opposed to plan officials, should be permitted to take advantage of the VFC Program as often as necessary without regard to the three year rule.

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EXHIBIT 1 PROHIBITED TRANSACTION CLASS EXEMPTION 2002-51, Continued

The commenter stated that subjecting service providers to the three year rule would not, in all cases, further the rule's purpose of ensuring that relief is not provided to fiduciaries who repeatedly make the same legal mistake. In contrast to plan sponsors, for example, service providers such as broker-dealers, banks and insurance companies may engage in numerous transactions with plans each day which could be prohibited except for the availability of a statutory or administrative exemption. The commenter noted that, if the plan fiduciary directing the transaction is relying on an exemption to deal with a party in interest, and that fiduciary is factually incorrect on an element of the exemption, the broker-dealer may engage in many transactions that would need relief under this exemption.

As an example, the commenter explained that a service provider could enter into a transaction that otherwise would be prohibited based on a fiduciary's representation that the QPAM class exemption (PTE 84-14) (49 FR 9494, March 13, 1984) applied. The QPAM class exemption requires, among other things, that neither the QPAM, an affiliate, nor any owner of a 5% or more interest in the QPAM, have been convicted or released from imprisonment as a result of certain crimes within the ten years immediately preceding the transaction. Information regarding past crimes of affiliates and 5% owners of the QPAM is not likely to be within the knowledge of the service provider, and the service provider must rely on the QPAM for assurance that the condition is satisfied.

The commenter suggested that Section II.F. be modified to provide an exception from the three year rule for applicants that are banks, broker-dealers or insurance companies (or affiliates thereof) which did not exercise discretionary authority or control to cause the plan to enter into the transaction. The commenter proposed that the exception be limited to applicants that were parties in interest (including fiduciaries) solely by reason of providing services to the plan (or solely by reason of a relationship to such service provider described in section 3(14)(F), (G), (H), or (I) and the corresponding provisions of the Code), and that "did not believe that an exemption was unavailable" with respect to the transaction. The commenter suggested that the applicant must have established written policies and procedures reasonably designed to ensure compliance with the prohibited transaction rules, and have engaged in periodic monitoring for compliance, at the time of the transaction.

The Department agrees that, in the narrow circumstances described above, such service providers should not be excluded from obtaining relief under the exemption by the three year rule. Accordingly, the Department has modified Section II.F. to clarify that the exemption will continue to be available notwithstanding the applicant's inability to satisfy the three year rule, provided that:

. The applicant was a broker-dealer registered under the Securities Exchange Act of 1934, a bank supervised by the United States or a State thereof, a broker-dealer or bank subject to foreign government regulation, an insurance company qualified to do business in a State, or any affiliate thereof;

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EXHIBIT 1 PROHIBITED TRANSACTION CLASS EXEMPTION 2002-51, Continued

. The applicant was a party in interest (including a fiduciary) solely by reason of providing services to the plan or solely by reason of a relationship to such service provider described in section 3(14)(F), (G), (H) or (I) (and/or the corresponding provisions of section 4975 of the Code);

. Neither the applicant nor any affiliate (i) was a fiduciary (within the meaning of section 3(21)(A) of ERISA) with respect to the assets of the plan involved in the transaction, and (ii) used its discretion to cause the plan to engage in the transaction;

. The individuals acting on behalf of the applicant in connection with the transaction had no actual knowledge or reason to know that the transaction was not exempt pursuant to a statutory or administrative exemption under ERISA and/or the Code; and

. Prior to the transaction, the applicant established written policies and procedures that were reasonably designed to ensure compliance with the prohibited transaction rules and the applicant engaged in periodic monitoring for compliance.

3. Participant Loan Repayments

The Department has made one additional modification to the final exemption. As discussed more fully below, the exemption provides relief for certain transactions described in the VFC Program, including the failure to transmit participant contributions to a pension plan within the time frames described in the Department's regulations at 29 CFR 2510.3-102. Subsequent to the publication of the final VFC Program, the Department issued guidance stating that applicants may correct the failure to forward participant loan repayments to a plan in a timely fashion under the VFC Program in the same manner. n2 Accordingly, the Department revised the language of Section I.A. of the exemption to explicitly cover the failure to transmit participant loan repayments to a pension plan within a reasonable time after withholding or receipt by the employer.

n2 See Frequently Asked Questions on the VFC Program, at http://www.dol.gov/pwba/faqs/faq-vfcp2.html. For the Department's views on the time frames for repayment of participant loans to pension plans, see the preamble to the final participant contribution regulation, 29 CFR section 2510.3-102, published at 61 FR 41220, 41226 (August 7, 1996). See also DOL Advisory Opinion No. 2002-02A (May 17, 2002).

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EXHIBIT 1 PROHIBITED TRANSACTION CLASS EXEMPTION 2002-51, Continued

Description of the Exemption

1. Scope

The exemption provides relief from the sanctions imposed under section 4975(a) and (b) of the Code, by reason of section 4975(c)(1)(A) through (E) of the Code, for certain eligible transactions identified in the VFC Program. The exemption does not provide relief for any transactions identified in the VFC Program that are not specifically described as eligible transactions under Section I of the exemption.

The four eligible transactions described in the exemption are as follows:

(A) The failure to transmit participant contributions to a pension plan within the time frames described in the Department's regulations at 29 CFR section 2510.3-102 and/or the failure to transmit participant loan repayments to a pension plan within a reasonable time after withholding or receipt by the employer.

(B) The making of a loan by a plan at a fair market interest rate to a party in interest with respect to the plan.

(C) The purchase or sale of an asset (including real property) between a plan and a party in interest at fair market value.

(D) The sale of real property to a plan by the employer and the leaseback of such property to the employer, at fair market value and fair market rental value, respectively.

The eligible transactions may be illustrated by the following examples:

Example (1): Corporation A sponsors a pension plan for its employees. Corporation A borrowed $ 100,000 from the plan. The loan was made at an interest rate no less than that available for a loan with similar terms (for example, the amount of the loan, amount and type of security, repayment schedule, and duration of loan) obtainable in an arm's-length transaction between unrelated parties. Example (2): Corporation B sponsors a pension plan for its employees. The plan sold a parcel of real property to Corporation B. The price Corporation B paid to the plan was the fair market value of the property as determined by a qualified independent appraiser as of the date of the transaction and reflected in a qualified appraisal report. (If there is a generally recognized market for the property, such as the New York Stock Exchange, the fair market value of the property is the value objectively determined by reference to the price on such market on the date of the transaction, and a determination by a qualified independent appraiser is not required.)

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EXHIBIT 1 PROHIBITED TRANSACTION CLASS EXEMPTION 2002-51, Continued

Example (3): Corporation C sponsors a pension plan for its employees. Corporation C sold a parcel of real property to the plan, which was simultaneously leased back to Corporation C. The price paid by the plan for the property was its fair market value, and the rent paid by Corporation C to the plan is the fair market rental value, as determined by a qualified independent appraiser and reflected in a qualified appraisal report. The terms of the lease (for example, rent, duration and allocation of expenses) are not less favorable to the plan than those obtainable in an arm's-length transaction between unrelated parties.

2. General Conditions

Section II of the exemption contains general conditions, as discussed below, which the Department views as necessary to ensure that any transaction covered by the exemption would be in the interests of plan participants and beneficiaries, and to support a finding that the exemption met the statutory requirements of section 4975(c)(2) of the Code.

With respect to a transaction involving delinquent transmittal of participant contributions and/or participant loan repayments to a pension plan, the exemption requires that the contributions or repayments be transmitted to the pension plan not more than 180 calendar days from the date the amounts were received by the employer (in the case of amounts that a participant or beneficiary pays to an employer) or the date the amount otherwise would have been payable to the participant in cash (in the case of amounts withheld by an employer from a participant's wages).

Second, the exemption requires that, with respect to the transactions described in Sections I.B., I.C. and I.D., the amount of plan assets involved in the transaction did not exceed 10 percent of the fair market value of all the assets of the plan at the time of the transaction. For purposes of this requirement, the 10 percent limitation would apply after aggregating the value of a series of related transactions.

Third, under the exemption, the fair market value of any plan asset involved in a transaction described in Sections I.C. or I.D. must have been determined in accordance with section 5 of the VFC Program. Section 5 of the VFC Program requires that the valuation meet the following conditions:

(1) If there is a generally recognized market for the property (e.g., the New York Stock Exchange), the fair market value of the asset is the average value of the asset on such market on the applicable date, unless the plan document specifies another objectively determined value (e.g., the closing price); and

(2) if there is no generally recognized market for the asset, the fair market value of that asset must be determined in accordance with generally accepted appraisal standards by a qualified independent appraiser and reflected in a written appraisal report signed by the appraiser.

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EXHIBIT 1 PROHIBITED TRANSACTION CLASS EXEMPTION 2002-51, Continued

For purposes of these requirements under the VFC Program, an appraiser is considered qualified if the appraiser has met the education, experience and licensing requirements that are generally recognized for appraisal of the type of asset being appraised. An appraiser is "independent" if the appraiser is not one of the following, does not own or control any of the following, and is not owned or controlled by, or affiliated with, any of the following: (i) The prior owner of the asset, if the asset was purchased by the plan; (ii) the purchaser of the asset, if the asset was or is now being sold by the plan; (iii) any other owner of the asset, if the plan is not the sole owner; (iv) a fiduciary of the plan; (v) a party in interest with respect to the plan (except to the extent the appraiser becomes a party in interest when retained to perform this appraisal for the plan); or (vi) the VFC Program applicant.

Fourth, under the exemption, the terms of a transaction described in Sections I.B., I.C., or I.D., must have been at least as favorable to the plan as the terms generally available in arm's-length transactions between unrelated parties.

Fifth, with respect to all of the eligible transactions, the transaction may not have been part of an agreement, arrangement or understanding designed to benefit a party in interest. The Department notes that the intent of this condition is not to deny a direct benefit to the party in interest but, rather, to exclude relief for transactions that are part of a broader overall agreement, arrangement or understanding designed to benefit parties in interest.

Sixth, with respect to all of the eligible transactions, the applicant may not have taken advantage of the relief provided by the VFC Program and the exemption for a similar type of transaction identified in the application during the three-year period prior to the submission of the application. As modified, however, the final exemption contains a limited exception from this condition for service providers. Pursuant to the amended Section II.F., a broker-dealer, bank or insurance company that is a service provider to a plan would not be subject to this condition if it engaged in a prohibited transaction described in Section I, provided that: it was not a fiduciary that used its discretion to cause the plan to engage in the transaction; individuals acting on its behalf in connection with the transaction had no actual knowledge or reason to know that the transaction was not exempt pursuant to a statutory or administrative exemption under ERISA and/or the Code; and, prior to the transaction, it established written policies and procedures that were reasonably designed to ensure compliance with the prohibited transaction rules and it engaged in periodic monitoring for compliance.

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EXHIBIT 1 PROHIBITED TRANSACTION CLASS EXEMPTION 2002-51, Continued

3. Compliance with VFC Program

In addition to compliance with the general conditions set forth above, Section III of the exemption requires that the applicant meet the requirements set forth in the VFC Program that are applicable to the particular transaction. The exemption also requires that the applicant have received a no action letter issued by PWBA with respect to such transaction, which must be an eligible transaction otherwise described in Section I of the exemption. However, the fact that an applicant receives a no action letter issued by PWBA should not be viewed as a determination by PWBA that the applicant has satisfied all of the conditions of the exemption. Each applicant must determine whether the pertinent conditions of the exemption have been met.

4. Notice

Notice under the exemption must be given to interested persons within 60 calendar days following the date of the submission of an application under the VFC Program to the Department. Plan assets may not be used to pay for the notice. The exemption does not specify the format or specific content of the notice. However, the notice must include an objective description of the transaction and the steps taken to correct it, written in a manner reasonably calculated to be understood by the average plan participant or beneficiary. The notice also must provide for a period of 30 calendar days, beginning on the date the notice is distributed, for interested persons to provide comments to the appropriate Regional Office of the United States Department of Labor, Pension and Welfare Benefits Administration. The notice must include the address and telephone number of such Regional Office.

A copy of the notice to interested persons, along with an indication of the date on which it was distributed, must be provided to the appropriate Regional Office within the same 60-day period following the date of the submission of the application. Accordingly, applicants under the VFC Program who intend to take advantage of the relief provided under this exemption would indicate on the checklist submitted as part of the VFC Program application that they will, within 60 calendar days following the date of the submission of the application, provide the Department's Regional Office with a copy of the notice to interested persons.

Notice may be given in any manner that is reasonably calculated, taking into consideration the particular circumstances of the plan, to result in the receipt of such notice by interested persons, including but not limited to posting, regular mail, or electronic mail, or any combination thereof.

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EXHIBIT 1 PROHIBITED TRANSACTION CLASS EXEMPTION 2002-51, Continued

General Information

The attention of interested persons is directed to the following:

(1) The fact that a transaction is the subject of an exemption under section 4975(c)(2) of the Code does not relieve a fiduciary or other party in interest or disqualified person with respect to a plan from certain other provisions of ERISA and the Code, including any prohibited transaction provisions to which the exemption does not apply, the requirement that all assets of an employee benefit plan be held in trust by one or more trustees, and the general fiduciary responsibility provisions of ERISA which require, among other things, that a fiduciary discharge his or her duties respecting the plan solely in the interests of the participants and beneficiaries of the plan and in a prudent fashion; nor does it affect the requirement of section 401(a) of the Code that the plan must operate for the exclusive benefit of the employees of the employer maintaining the plan and their beneficiaries.

(2) The exemption does not extend to transactions prohibited under section 4975(c)(1)(F) of the Code.

(3) In accordance with section 4975(c)(2) of the Code, the Department finds that the exemption is administratively feasible, in the interests of plans and their participants and beneficiaries, and protective of the rights of participants and beneficiaries of such plans.

(4) The exemption is supplemental to, and not in derogation of other provisions of ERISA and the Code, including statutory or administrative exemptions and transitional rules. Furthermore, the fact that a transaction is subject to an administrative or statutory exemption is not dispositive of whether the transaction is in fact a prohibited transaction.

(5) The exemption is applicable to a transaction only if the conditions specified in the class exemption are satisfied.

Exemption

Accordingly, the following exemption is granted under the authority of section 4975(c)(2) of the Code, and in accordance with the procedures set forth in 29 CFR part 2570, subpart B (55 FR 32836, 32847, August 10, 1990).

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EXHIBIT 1 PROHIBITED TRANSACTION CLASS EXEMPTION 2002-51, Continued

Section I: Eligible Transactions

The sanctions resulting from the application of section 4975(a) and (b) of the Code, by reason of section 4975(c)(1)(A) through (E) of the Code, shall not apply to the following eligible transactions described in section 7 of the Voluntary Fiduciary Correction (VFC) Program (67 FR 15061, March 28, 2002), provided that the applicable conditions set forth in Sections II, III and IV are met:

A. Failure to transmit participant contributions to a pension plan within the time frames described in the Department's regulation at 29 CFR section 2510.3-102, (see VFC Program, section 7.A.1.), and/or the failure to transmit participant loan repayments to a pension plan within a reasonable time after withholding or receipt by the employer.

B. Loan at a fair market interest rate to a party in interest with respect to a plan. (See VFC Program, section 7.B.1.).

C. Purchase or sale of an asset (including real property) between a plan and a party in interest at fair market value. (See VFC Program, sections 7.C.1. and 7.C.2.).

D. Sale of real property to a plan by the employer and the leaseback of the property to the employer, at fair market value and fair market rental value, respectively. (See VFC Program, section 7.C.3.).

Section II: Conditions

A. With respect to a transaction involving participant contributions or loan repayments to pension plans described in Section I.A., the contributions or repayments were transmitted to the pension plan not more than 180 calendar days from the date the amounts were received by the employer (in the case of amounts that a participant or beneficiary pays to an employer) or the date the amounts otherwise would have been payable to the participant in cash (in the case of amounts withheld by an employer from a participant's wages).

B. With respect to the transactions described in Sections I.B., I.C., or I.D., the plan assets involved in the transaction, or series of related transactions, did not, in the aggregate, exceed 10 percent of the fair market value of all the assets of the plan at the time of the transaction.

C. The fair market value of any plan asset involved in a transaction described in Sections I.C. or I.D. was determined in accordance with section 5 of the VFC Program.

D. The terms of a transaction described in Sections I.B., I.C., or I.D. were at least as favorable to the plan as the terms generally available in arm's-length transactions between unrelated parties.

Continued on next page

EXHIBIT 1 PROHIBITED TRANSACTION CLASS EXEMPTION 2002-51, Continued

E. With respect to any transaction described in Section I, the transaction was not part of an agreement, arrangement or understanding designed to benefit a party in interest.

F. (1) With respect to any transaction described in Section I, the applicant has not taken advantage of the relief provided by the VFC Program and this exemption for a similar type of transaction(s) identified in the current application during the period which is three years prior to submission of the current application.

(2) Notwithstanding the foregoing, Section II.F.(1) shall not apply to an applicant provided that:

(a) The applicant was a broker-dealer registered under the Securities Exchange Act of 1934, a bank supervised by the United States or a State thereof, a broker-dealer or bank subject to foreign government regulation, an insurance company qualified to do business in a State, or an affiliate thereof;

(b) The applicant was a party in interest (including a fiduciary) solely by reason of providing services to the plan or solely by reason of a relationship to such service provider described in section 3(14)(F), (G), (H) or (I) (and/or the corresponding provisions of section 4975 of the Code);

(c) Neither the applicant nor any affiliate (i) was a fiduciary (within the meaning of section 3(21)(A) of ERISA) with respect to the assets of the plan involved in the transaction and (ii) used its discretion to cause the plan to engage in the transaction;

(d) Individuals acting on behalf of the applicant had no actual knowledge or reason to know that the transaction was not exempt pursuant to a statutory or administrative exemption under ERISA and/or the Code; and

(e) Prior to the transaction, the applicant established written policies and procedures that were reasonably designed to ensure compliance with the prohibited transaction rules and the applicant engaged in periodic monitoring for compliance.

Section III: Compliance with VFC Program

A. The applicant has met all of the applicable requirements of the VFC Program.

B. PWBA has issued a no action letter to the applicant pursuant to the VFC Program with respect to a transaction described in Section I.

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EXHIBIT 1 PROHIBITED TRANSACTION CLASS EXEMPTION 2002-51, Continued

Section IV: Notice

A. Written notice of the transaction(s) for which the applicant is seeking relief pursuant to the VFC Program and this exemption, and the method of correcting the transaction, was provided to interested persons within 60 calendar days following the date of the submission of an application under the VFC Program. A copy of the notice was provided to the appropriate Regional Office of the United States Department of Labor, Pension and Welfare Benefits Administration within the same 60-day period, and the applicant indicated the date upon which notice was distributed to interested persons. Plan assets were not used to pay for the notice. The notice included an objective description of the transaction and the steps taken to correct it, written in a manner reasonably calculated to be understood by the average plan participant or beneficiary. The notice provided for a period of 30 calendar days, beginning on the date the notice was distributed, for interested persons to provide comments to the appropriate Regional Office. The notice included the address and telephone number of such Regional Office.

B. Notice was given in a manner that was reasonably calculated, taking into consideration the particular circumstances of the plan, to result in the receipt of such notice by interested persons, including but not limited to posting, regular mail, or electronic mail, or any combination thereof. The notice informed interested persons of the applicant's participation in the VFC Program and intention of availing itself of relief under the exemption.

Signed at Washington, DC, this 11th day of November, 2002.

Ivan L. Strasfeld,

Director of Exemption Determinations, Pension and Welfare Benefits Administration, U.S. Department of Labor.

EXHIBIT 2 ANNOUNCEMENT 2002-31

On March 15, 2000, the U.S. Department of Labor (the "DOL") published at 65 Fed. Reg. 14164, its interim Voluntary Fiduciary Correction ("VFC") program. The DOL has adopted its permanent VFC program. In conjunction with that program, the DOL, which, generally, has the authority to determine whether a transaction is prohibited under §4975 of the Internal Revenue Code, published a notice of a proposed class exemption (Application No. D-10933) from the prohibited transaction rules pertaining to four of the enumerated transactions that come under the VFC program.

The proposed class exemption when finalized will provide relief from the sanctions of §4975(a) and (b) of the Internal Revenue Code, i.e., the application of the excise taxes described therein applied as a result of §4975(c)(1)(A) through (E), [1] with respect to the four enumerated transactions. Among the conditions for an applicant to be eligible for the proposed class exemption are the following: (1) meeting the requirements of the VFC program pertaining to the particular transaction, (2) receiving a No Action Letter from the DOL regarding the transaction, and (3) providing notice to all interested persons.

The Service recognizes that a disqualified person who meets the conditions described in the proposed class exemption could nevertheless be subject to the sanctions of §4975 during the pendency of the proposed class exemption despite the fact that the proposed class exemption when finalized will cause those sanctions not to apply with respect to the transactions enumerated in the class exemption (assuming all of the conditions of the class exemption are met). In order to encourage fiduciaries that meet the terms of the proposed class exemption to participate in the DOL's VFC program and to remove a significant disincentive from participating in that program, the Service will not seek to impose the §4975(a) and (b) excise taxes with respect to any prohibited transaction that is covered by the proposed class exemption notwithstanding any subsequent changes to the proposed class exemption when it is finalized, provided that all of the requirements specified in the proposed class exemption are met.

Drafting Information

The principal author of this announcement is Michael Rubin of the Tax Exempt and Government Entities Division, Employee Plans. For further information regarding this announcement, please contact the Employee Plans' taxpayer assistance telephone service at 1-877-829-5500 (a toll-free number), between the hours of 8:00 a.m. and 6:30 p.m. Eastern Time, Monday through Friday. Mr. Rubin can be contacted at 202-283-9888 (not a toll-free number).

[1] The prohibited transactions described in §4975(c)(1)(F), i.e., the receipt of any consideration for his or her own personal account by any disqualified person who is a fiduciary from any party dealing with the plan in connection with a transaction involving the income or assets of the plan, does not come within the framework of the DOL's proposed class exemption or this announcement.

EXHIBIT 3 Adoption of Voluntary Fiduciary Correction Program [03/28/2002]

Volume 67, Number 60, Page 15061-15083

DEPARTMENT OF LABOR

Pension and Welfare Benefits Administration

RIN 1210-AA76

Adoption of Voluntary Fiduciary Correction Program

AGENCY: Pension and Welfare Benefits Administration, Labor.

SUMMARY: The Department of Labor adopts the Voluntary Fiduciary Correction Program (VFC Program or Program) by the Department of Labor's Pension and Welfare Benefits Administration (PWBA). The VFC Program allows certain persons to avoid potential Employee Retirement Income Security Act of 1974, as amended (ERISA), civil actions initiated by the Department of Labor and the assessment of civil penalties under section 502(l) of ERISA in connection with investigation or civil action by the Department. The VFC Program is designed to benefit workers by encouraging the voluntary and timely correction of possible fiduciary breaches of Part 4 of Title I of ERISA.

EFFECTIVE DATE: April 29, 2002.

ADDRESSES: Address questions regarding specific applications for relief under the VFC Program to the appropriate PWBA Regional Office listed in Appendix C.

FOR FURTHER INFORMATION CONTACT: For Specific Applications Under the VFC Program: Contact the appropriate PWBA Regional Office listed in Appendix C.

For General Questions Regarding the VFC Program: Contact the appropriate PWBA Regional Office listed in Appendix C or Jeffrey A. Monhart, Lead Investigator, Office of Enforcement, Pension and Welfare Benefits Administration, U.S. Department of Labor, Washington, DC, (202) 693-8454, or Elizabeth A. Goodman, Pension Law Specialist, Office of Regulations and Interpretations, Pension and Welfare Benefits Administration, U.S. Department of Labor, Washington, DC, (202) 693-8510. (These are not toll-free numbers.)

SUPPLEMENTARY INFORMATION:

Discussion of the Program and Comments

Background

Title I of ERISA, 29 U.S.C. section 1001 et seq., establishes certain standards with which officials of employee benefit plans covered by ERISA must comply. PWBA helps the public to understand the requirements of Title I of ERISA. In addition, PWBA conducts investigations to deter and correct violations of ERISA. Based on PWBA's experience with the Pension Payback Program, 61 FR 9203 (March 7, 1996) (Pension Payback Program), and continued public interest in such programs, PWBA decided to establish the VFC Program on an interim basis (Interim VFC Program). The Interim VFC Program was published in the Federal Register on March 15, 2000 (65 FR 14164), and has been administered out of each of PWBA's ten regional offices since April 14, 2000. The VFC Program is designed to assist Plan Officials (as defined in Section 3) by specifying the steps necessary to correct certain potential violations of Title I of ERISA. Based on its experience with administering the Program on an interim basis and the public comments received, PWBA has decided to implement the Program on a permanent basis. The Program will continue to be operated out of the ten regional PWBA offices.

Section 409 of ERISA provides that a fiduciary who breaches any of the responsibilities, obligations, or duties imposed upon fiduciaries by Part 4 of Title I of ERISA shall be personally liable to make good to a plan any losses to the plan resulting from each breach, and to restore to the plan any profits of such fiduciary which have been made through the use of assets of the plan by the fiduciary. Where more than one fiduciary is liable for a breach, liability is joint and several. The Secretary of Labor has the authority, under sections 502(a)(2) and 502(a)(5), to bring civil actions to enforce the provisions of Title I of ERISA. Section 502(l) requires the assessment of a civil penalty in an amount equal to 20 percent of the amount recovered under any settlement agreement with the Secretary or ordered by a court in an action initiated by the Secretary under section 502(a)(2) or 502(a)(5) with respect to any breach of fiduciary responsibility under (or other violation of) Part 4 by a fiduciary. Under section 502(l)(1)(B), this civil penalty also is assessed against knowing participants in a breach.

PWBA believes that the possibility of investigation, commencement of a civil action, and imposition of a civil penalty under section 502(l) of ERISA may constrain persons who have engaged in a possible breach of fiduciary responsibility under Part 4 of Title I of ERISA from identifying themselves and working with PWBA to correct the breach fully and make the plan whole. To encourage the full correction of certain breaches of fiduciary responsibility and the restoration to participants and beneficiaries of losses resulting from those breaches, PWBA has decided to implement the VFC Program on a permanent basis. Under the Program, persons who are potentially liable for a breach are relieved of the possibility of civil investigation of that breach and/or civil action by the Secretary with respect to that breach, and imposition of civil penalties under section 502(l), if they satisfy the conditions for correcting the breach as described in the VFC Program.

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EXHIBIT 3 Adoption of Voluntary Fiduciary Correction Program [03/28/2002], Continued

If a person files an application under the VFC Program, but the corrective action falls short of a complete and acceptable correction, PWBA may reject the application and pursue enforcement, including assessment of a section 502(l) penalty. However, no section 502(l) penalty would be imposed on any amounts already restored to the plan by the applicant prior to filing the VFC Program application. The penalty would only apply to the additional recovery amount, if any, paid to the plan pursuant to a court order or a settlement agreement with the Department.

The March 15, 2000 Interim VFC Program

The Interim VFC Program was set forth in seven sections and three appendices. It was structured to maximize the ability of Plan Officials to identify and correct possible breaches that are within the scope of the Program without the need to consult with PWBA. As noted in Section 1, Purpose and Overview of the Voluntary Fiduciary Correction Program, PWBA believed that the VFC Program would assist Plan Officials in understanding the requirements of Part 4 of Title I of ERISA and would facilitate the correction of transactions and the restoration of losses to employee benefit plans resulting from fiduciary breaches.

Section 2, Effect of the VFC Program, made clear that the applicant must be careful to ensure that the eligibility requirements are met and the corrections specified for individual transactions are performed before an application is filed under the VFC Program. Generally, if an applicant is in full compliance with all of the terms and procedures set forth in the VFC Program, PWBA will issue a ``no action letter'' in the format shown in Appendix A with respect to the breach described in the application. Relief under the Interim VFC Program was limited to the transactions identified in the application and to the persons who corrected those transactions. In certain cases, such as where PWBA might become aware of possible criminal behavior, material misrepresentations or omissions in the VFC Program application, or other abuse of the VFC Program, relief would not be available under the Interim VFC Program. In those cases, the Department reserved the right to initiate an investigation, which could lead to enforcement action. PWBA expected that such cases would be unusual. Full correction under the Interim VFC Program did not preclude any other governmental agency, including the Internal Revenue Service (IRS), from exercising any rights it might have had with respect to the transactions that were the subject of an application. PWBA sought comments on possible areas of coordination between PWBA and the IRS that would facilitate voluntary correction of breaches of Title I of ERISA. PWBA noted that based on its preliminary review of the VFC Program, the IRS had indicated that except in those instances where the fiduciary breach or its correction results in a tax abuse situation or a plan qualification failure, a correction under this Program generally would be acceptable under the Internal Revenue Code.

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The Interim VFC Program was designed to address a wide variety of situations where plans have been harmed as a result of possible breaches of fiduciary duty. Section 3, Definitions, made clear that a transaction may be corrected without a determination that there is an actual breach; there need only be a possible breach. In addition, persons who may correct a fiduciary breach include not only any breaching fiduciary, but also plan sponsors, parties in interest or other persons in a position to correct a breach. However, the definition of Under Investigation, along with the criteria set forth in Section 4, Program Eligibility, provided that persons or plans who are the subject of pending investigations for violations of Title I of ERISA, or who appear to have engaged in criminal violations, could not take advantage of the VFC Program. Further, PWBA reserved the right to reject an application when warranted by the facts and circumstances of a particular case.

The Interim VFC Program noted that PWBA believes that it must assess a penalty under section 502(l) of ERISA to the extent that it negotiates relief owed to the plan as a result of a transaction in exchange for a no action letter to the potentially liable persons. Accordingly, the Interim VFC Program was structured so that applicants have the maximum information available to identify eligible transactions and make complete and fully acceptable corrections without discussion or negotiation with the Department.

Section 5, General Rules for Acceptable Correction, set forth issues that are likely to be present with regard to any transaction described in Section 7. For example, Section 5 described how fair market value determinations must be made, how correction amounts must be determined, and what documentation is required for all applications. Section 5 also made clear that the cost of correction must be borne by the applicant and not the plan. In addition, Section 5 stated when notice must be provided to participants and when former employees who have already been cashed out of a plan must also be included in any amount restored to a plan.

Section 6, Application Procedures, specified the requirements for the application, including documentation and the penalty of perjury statement that must be signed by a plan fiduciary with knowledge of the transaction and the applicant's authorized representative, if any. Section 6 was supplemented by Appendix B, the VFC Program Checklist that was designed to help the applicant determine whether he or she has met all of the application requirements, including all necessary documentation, prior to submission to PWBA.

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Section 7, Description of Eligible Transactions and Methods of Correction, set forth five types of transactions that may be corrected pursuant to the VFC Program. The first, ``Delinquent Participant Contributions to Pension Plans,'' was included in the Interim VFC Program based on PWBA's experience with the Pension Payback Program. Unlike the Pension Payback Program, the Interim VFC Program did not exempt from excise taxes any violations of section 4975 of the Internal Revenue Code (the Code). PWBA included the other types of transactions based on its enforcement experience. For the interim stage of the VFC Program, PWBA took a conservative approach and limited the eligible transactions to those where the nature of the transaction and the required correction could be described accurately without reference to specific circumstances, and thus could be corrected satisfactorily without consultation and negotiation with PWBA. PWBA sought comments on whether different correction methods or earnings calculation methods should be available in the Program.
Comments on the Interim VFC Program

In General

In general, comments received on the VFC Program were favorable. Commenters expressed support for a formal program that encourages identification and correction of potential breaches of fiduciary duty. Among the advantages cited were increased fiduciary oversight of plans, reduction of litigation costs, and security of benefits. Some commenters represented generally, however, that the VFC Program contains disincentives to participation. Other commenters stated that Section 2(c)(6) (Other actions not precluded) will deter potential applicants. These comments noted that Section 2(c)(6) does not preclude PWBA from seeking injunctive relief against any person responsible for a transaction, referring information concerning the transaction to the IRS, or imposing civil penalties under section 502(c)(2) of ERISA. Commenters also pointed out that other parties, including participants, could file suit against applicants. Several comments observed that PWBA reserves the right to reject an application if the facts and circumstances warrant, and that PWBA may initiate a civil or criminal investigation in certain cases. Commenters suggested these provisions might discourage potential applicants from participating in the Program.

Several commenters expressed concern that the Department might target VFC Program applicants for investigation. Commenters believe that the lingering risk of enforcement action creates a disincentive for potentially liable parties to identify themselves to the Department. These comments suggested that the Department should offer public assurances that applicants will not be investigated. The commenters also questioned whether the Department would target an applicant plan for other potential violations for which VFC Program relief had not been requested. Commenters suggested the Department should offer VFC Program relief for violations of sections 403 and 404(a) of ERISA if those violations relate to a transaction corrected under the Program.

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PWBA believes that the benefits of participating in the VFC Program should outweigh any concern about possible enforcement by the Department in response to an application. As noted in the preamble to the Interim VFC Program, the Department generally does not anticipate taking enforcement action in response to an application except in the unusual situation where PWBA becomes aware of possible criminal behavior, material misrepresentations or omissions in the VFC Program application, or other abuse of the Program. Moreover, although the VFC Program does not provide specifically for relief from violations of section 403 and 404 of ERISA, the Department anticipates that as a general matter applicants will have corrected violations of section 403 and 404 that are integrally related to transactions corrected under the Program. PWBA continues to believe, however, that transactions violative of section 403 and 404 are not appropriate for the Program because unlike the transactions selected for the Program, the nature of the corrections required for violations of sections 403 and 404 will vary under the facts and circumstances of the particular transactions, and thus, proper correction is likely to require negotiations subject to the section 502(l) penalty. PWBA encourages plan officials who discover a transaction that is a breach of both section 404 and 406 to make full correction under the Program and to take any additional action necessary to correct the section 404 violations in conjunction with the appropriate regional office. PWBA emphasizes in this regard that only amounts actually negotiated as settlement in excess of those paid under the VFC Program, or otherwise paid to the plan by the correcting officials after discussion with PWBA, are potentially subject to section 502(l) penalties.

Specific Comments

Excise Tax Relief

Several commenters requested that the VFC Program be amended to provide for relief from excise taxes in addition to the Program's relief from ERISA section 502(l) penalties. Commenters noted that the Department granted relief from excise taxes in its Pension Payback Program. Commenters stated that they believed that the possibility of referral by the Secretary of Labor to the Internal Revenue Service as mandated by section 3003 of ERISA and the absence of any relief under the VFC Program from the Code's requirement that excise taxes be paid in full for the transactions at issue would provide significant disincentives for participating in the Program.

As discussed in more detail in the preamble to the Notice of Proposed Class Exemption, published in this issue of the Federal Register simultaneously with the adoption of the VFC Program (Class Exemption),\1\ PWBA has determined that limited excise tax relief is appropriate for the correction of certain transactions under the Program.

\1\ All references to the Class Exemption hereafter include the Proposed Class Exemption until finalized.

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PWBA also notes that applicants who would not otherwise be liable for excise taxes under section 4975(a) of the Code, but who are in a position to correct a breach, are not made liable for excise taxes solely by virtue of their participation in the Program.

Notice to Participants

The majority of commenters requested that PWBA eliminate or reduce the notice requirements in Section 5, General Rules for Acceptable Corrections. Commenters noted that the Department generally does not require notice of correction to participants when the Department resolves investigations through voluntary compliance or lawsuits. Commenters stated that the notice requirement might invite participant litigation concerning the transaction described in a VFC Program application. Other commenters maintained that notice of the correction might erode employee morale, and that participants would receive sufficient notice simply by observing any increase in their account balance. One commenter explicitly supported the notice requirement in the Interim VFC Program.

PWBA believes that informed participants promote the goals of sound plan administration and protection of benefits. PWBA agrees, however, that the original notice requirements could discourage correction through participation in the VFC Program, and therefore eliminate opportunities to protect and restore plan benefits. Accordingly, in the permanent VFC Program, PWBA has omitted those notice requirements specified in section 5(e) of the Interim VFC Program. To the extent that the applicant avails him or herself of excise tax relief under the Class Exemption, however, the notice requirements described therein must be followed. PWBA also expects that if correction under the Program involves an adjustment of account balances or supplemental distributions, the plan will explain to the affected participants and beneficiaries the basis for such adjustment or distribution.

Protection of Participant Privacy Data

Commenters objected to the fact that requiring production on request to participants of the entire application and supporting documents, which was part of the original notice requirement in section 5(e) of the Interim VFC Program, if read literally, could be interpreted to require the production of protected privacy data. Although the notice requirement, which included a notice of the right to obtain a copy of the application, has been eliminated from the Program, PWBA believes that participants have a right to obtain copies of the application and supporting documentation. PWBA believes that it would be required to produce portions of the application under the Freedom of Information Act. Therefore, such information will be made available by PWBA to any participant or beneficiary who formally seeks such information, but no privacy data that would be protected under law will be disclosed. PWBA encourages plan officials to give copies of applications directly to participants, but recognizes that privacy data need not be disclosed.

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Voluntary Self-Correction

A number of commenters suggested that PWBA expand the VFC Program to include voluntary self-correction similar to that in IRS Rev. Proc. 2001-16 (now Rev. Proc. 2001-17).\2\ These commenters suggested that the VFC Program provide that if a plan official were to correct a transaction in accordance with the Program without making an application, that PWBA would not take action against potentially liable parties if the transaction in question were discovered on audit. Commenters suggested that adding a self-correction option would encourage correction of minor technical breaches by plan officials and would obviate the need for PWBA to process applications for such types of transactions.

\2\ The Interim VFC Program referred to IRS Rev. Proc. 2000-16. IRS Rev. Proc. 2001-17 superceded IRS Rev. Proc. 2000-16. For convenience, all references to the IRS correction programs and procedures are to IRS Rev. Proc. 2001-17 and include reference to any subsequent versions in future years.

PWBA has decided not to include a formal self-correction option in the VFC Program. PWBA believes that an important result under the VFC Program is certainty that applicants have complied with the terms of the Program and have revealed the details of the transaction and the correction under penalty of perjury. PWBA does not believe that it is possible to offer relief under the VFC Program without the opportunity to scrutinize details of the transaction and correction as would be provided in a formal application. Nonetheless, PWBA notes that an ERISA section 502(l) penalty is assessed only on amounts obtained pursuant to a settlement agreement with the Secretary or ordered by a court to be paid in a judicial proceeding instituted by the Secretary under subsection 502(a)(2) or (5). Accordingly, if a potentially liable party were to have corrected a transaction as specified by the Program and the transaction with the correction were later to be discovered on audit, any penalty to be assessed on an applicable recovery amount within the meaning of section 502(l) would be limited to any additional amount that might be required by PWBA to be paid following the audit.\3\

\3\ PWBA notes that if it discovered on audit a prohibited transaction that is subject to section 4975 of the IRC, it would have an obligation under section 3003 of ERISA to make a referral to the IRS. When plan officials desire to correct a prohibited transaction, plan officials should make sure they satisfy the requirements of both the Department of Labor and the IRS.

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Expansion of the VFC Program To Include Additional Transactions

PWBA sought input from the public on whether the VFC Program should be expanded to include additional transactions. Some commenters believed that the VFC Program should not be limited to specific transactions, but rather should include all types of fiduciary breaches. Other commenters suggested that certain specific transactions be added to the VFC Program. These transactions included plan contracts that result in excessive surrender charges, losses due to a failure to monitor investments, failure to diversify plan investments and problems with Summary Plan Descriptions (SPDs), Form 5500s and qualified domestic relations order (QDRO) administration. PWBA believes that these transactions are not appropriate for the VFC Program because the adequacy of the correction depends on facts and circumstances and therefore is not sufficiently uniform to be described in the Program in a manner that would obviate the need for any negotiation to ensure full correction. In addition, a separate voluntary compliance program (the Delinquent Filer Voluntary Compliance Program) is maintained for resolution of annual reporting (Form 5500 series) compliance issues. After considering the comments, PWBA has decided to maintain the basic structure of the Interim VFC Program and limit relief to the transactions specified. PWBA believes that the transactions currently included in the Program represent those with respect to which plans will maximize recoveries by voluntary correction without requiring negotiation between applicants and the Department. The Program has been expanded to add correction of delinquent employee contributions to both insured and funded welfare plans. PWBA will continue to review the scope of the VFC Program as it gains more experience with administering the Program. In this regard, PWBA invites members of the public to submit additional comments on viable transactions and reasonable methods of correction through the VFC Program for those suggested transactions.

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Use of Alternative Correction Methods

PWBA requested input from the public on additional or different correction methods. Commenters generally favored having more flexibility in choosing correction options. After evaluating the comments, however, PWBA continues to believe that giving applicants complete flexibility in choosing correction methods will necessitate a level of review and negotiation by PWBA that would result in a settlement agreement within the meaning of ERISA section 502(l). Accordingly, PWBA will not make any changes to the VFC Program to permit alternative correction methods.

Use of New Prohibited Transactions as an Alternative Correction Method

One commenter suggested, with respect to proposed alternative correction methods, that the VFC Program permit engaging in a new prohibited transaction to correct the breach where the new prohibited transaction is the most viable way to correct the transaction that is the subject of the application. The Interim VFC Program contains correction methods that do not involve engaging in a new prohibited transaction because a new prohibited transaction would require exemptive relief or be subject to excise taxes.

Parties who believe that it is not feasible to correct a transaction through the VFC Program because the only viable correction, in the applicant's opinion, involves a new prohibited transaction may seek voluntary compliance with the Department outside of the VFC Program or may apply for individual relief from the prohibited transaction provisions for the new transaction from the Office of Exemption Determinations. In such circumstances, the corrected transaction would be subject to any applicable excise taxes and ERISA section 502(l) penalties, but the new transaction would not require the payment of excise taxes. PWBA notes in this regard that Prohibited Transaction Exemption 94-71 exempts from excise taxes new prohibited transactions that are used to correct a past transaction where the Department in a written settlement agreement approves the new prohibited transaction. However, PTE 94-71 does not relieve liable parties from excise taxes for the corrected transaction.

Proof of Payment to Missing Individuals Who Are Entitled to Distributions Under the VFC Program

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The correction procedures under the Interim VFC Program required applicants to provide evidence that all participants and beneficiaries entitled to an additional distribution have been paid. One commenter noted that it can take a significant amount of time to locate former employees who are not in current pay status with the plan, their beneficiaries, and alternate payees, and suggested that the Program be amended to provide, similar to the IRS correction programs in Rev. Proc. 2001-17, that the applicant be required only to demonstrate that it has segregated funds for missing individuals and is taking appropriate steps to locate and pay those individuals. PWBA agrees that requiring proof of payment to all entitled individuals could significantly delay an applicant's ability to obtain relief under the Program. PWBA therefore has amended Section 5(d) of the VFC Program to require proof of payment only to participants and beneficiaries whose current location is known to the plan and/or applicant. For missing individuals who need to be located, applicants need only demonstrate that they have segregated adequate funds to pay the missing individuals and demonstrate that they have commenced the process of locating those individuals using either the IRS and Social Security Administration locator services, or other comparable means.

Comments Suggesting Changes Where Correction Includes Distribution to Participants

One commenter suggested that because the cost of making the distribution may sometimes exceed the amount of the distribution, PWBA should use a ``reasonableness standard'' with some flexibility where either the costs of full correction exceed the actual benefit to the plan or it is impossible to make full correction. The Interim VFC Program did not have a de minimus exception for making required distributions. Another commenter suggested that the VFC Program be modified to take into account situations where the costs of correction exceed the benefit to the plan. The IRS Rev. Proc. 2001-17 has an exception for making required distributions where the amount of the distribution is less than $20 and the cost of the distribution exceeds the distribution.

PWBA has decided to amend the VFC Program by adding Section 5(e), De Minimus Exception, to parallel the IRS correction programs with respect to former employees, their beneficiaries and alternate payees who have neither account balances with, nor a right to future benefits, from the plan. Under the new section 5(e), where correction under the Program requires distributions to such individuals in amounts of less than $20 per individual, and the applicant demonstrates in its submission that the cost of making the distribution exceeds the cost of correction, the applicant need not make distributions to those individuals who have separated from the plan and who would receive less than $20 as part of the correction. Instead, the applicant need only make payment to the plan in the required amount and the payments will be treated as any other payments or credits to the plan that are not allocated to individual accounts.

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Another commenter noted that in situations where assets of the plan are overvalued, such as those situations described in section 7(d) of the Interim VFC Program, correction requires the applicant to make good the losses to the plan, without regard to whether assets are recovered from any participants or beneficiaries who might have received an overpayment. That commenter suggested that the VFC Program should be revised to allow plan fiduciaries first to attempt to collect any overpayment from a participant or beneficiary before the applicant is required to restore the amount overpaid to the plan. PWBA has determined not to amend the VFC Program in this regard. PWBA is concerned that encouraging applicants to pursue participants and beneficiaries for excess benefit payments will unduly delay making the plan whole.

Use of Alternative Earnings Calculations

PWBA also requested comments from the public on whether different earnings calculations might be appropriate to correct some or all of the transactions in the Program. Generally, commenters believed that alternative methods should be permitted so long as they provide adequate recovery. Some commenters believed that the methods described in the Program were too rigid. Others believed that certain of the methods provided more relief than could be obtained by the Department in litigation. Evaluation of alternative earnings calculations, however, would require discussions and negotiations between PWBA and the applicant. Thus, PWBA continues to believe that applicants must use the earnings calculation methods described in the VFC Program in order to obtain relief under the Program and has not amended the Program in this regard.

PWBA also received comments on certain specific aspects of the earnings calculations for the Program. PWBA notes that the correction methods, including earnings calculations in the Program, are fairly closely patterned on those in the IRS correction methods for prohibited transactions (see 26 CFR 53.4941(e)-1(c)) and in the IRS correction programs (Rev. Proc. 2001-17).

One commenter suggested that using the Internal Revenue Code section 6621 rate as a ``floor'' provided an inappropriate windfall to the plan. According to the commenter, profits made on the use of the plan funds rather than the loss to the plan should only be required where there is proof of a causal connection between the use of the funds and the profits gained by the breaching party. PWBA has determined not to amend the Program in this regard. Section 409 of ERISA provides that any person who is a fiduciary with respect to a plan who breaches any of the responsibilities, obligations, or duties imposed upon fiduciaries by this title shall be personally liable to make good to the plan any losses to the plan resulting from each breach, and to restore to the plan any profits of such fiduciary which have been made through the use of assets of the plan by the fiduciary. The VFC Program is structured to make the plan whole without the need for investigation and suit and the costs attendant thereto in exchange for relief from penalties under section 502(l).

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Another commenter suggested that for an ERISA section 404(c)-type plan, it would be more appropriate to use a blended rate, as opposed to the highest rate of return, if, for administrative convenience as was permitted under the Interim VFC Program, the applicant was not using the actual return an individual participant would have earned based on his or her investment allocations. PWBA notes that IRS Rev. Proc. 2001-17, Appendix B, permits IRS program applicants to use the highest rate of return for administrative convenience when adding funds to a plan participant's account as part of a correction. Rev. Proc. 2001-17 provides, however, that the employer correcting the violations may use the blended overall return for the plan only if a plan participant has not made any investment allocations and funds are being added to his or her account as part of the correction. PWBA has decided to amend Section 5(b)(5) of the VFC Program to track more closely the IRS correction programs. The VFC Program is modified to permit the use of a blended rate for affected participants who have not made any investment allocations. Where participants have made elections, the applicant must still either calculate the actual rate of return or use the investment with the highest rate of return among the designated broad range of investment alternatives available to the participants.

Certain commenters, as well as applicants who have participated in the Interim VFC Program, identified ambiguities in the earnings calculation methods for lost earnings with respect to delinquent participant contributions to pension plans. PWBA recognizes that calculating lost earnings, particularly for delinquent contributions to 401(k) plans, may be complicated, depending on the length of the delinquency, the number of investment options and the performance of those options. PWBA has elected not to change the VFC Program with respect to the earnings calculations; it believes that only a general formula will address the myriad situations that may arise. PWBA has however, slightly modified the examples to eliminate some references to annualized yields for short correction periods to lessen any possible confusion in applying the principles set forth in the examples. Nonetheless, PWBA recognizes that there may be situations, depending on the duration of the delinquency and the information available to the correcting officials regarding investment performance, where use of a fraction of an annualized yield may be appropriate.

Form 5500 Filings Associated With VFC Program

PWBA received several comments with respect to Form 5500 filings associated with the VFC Program. Commenters generally were concerned that they not be subject to penalties for improper filings if they filed an amended return in connection with the VFC Program. One commenter suggested that the Delinquent Filer Voluntary Compliance Program be consolidated with the VFC Program. Another commenter suggested that there be no penalties associated with any filings required by the VFC Program. One commenter suggested that PWBA eliminate any requirement for filing amended returns to reflect the transactions corrected by the VFC Program.

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PWBA has decided to keep the filing requirements associated with the VFC Program as published in the Interim VFC Program. PWBA believes that where a plan has engaged in a prohibited transaction or plan assets have been valued improperly, Forms 5500 must be amended to reflect these important reporting items. PWBA notes that filing an amended return for these purposes will not trigger a penalty, and accordingly, there is no need to provide special relief under section 502(c)(2). Penalties attach under section 502(c)(2) for delinquent and non-filers. If a plan has filed a return that is inadequate, PWBA can reject the return. If the filer does not correct the return within 45 days of rejection by the Office of the Chief Accountant, PWBA may then assess a penalty. PWBA does not anticipate that amended Forms 5500 filed to reflect transactions or valuations corrected in accordance with the terms of the VFC Program will be subject to rejection for those amendments alone.

The Delinquent Filer Voluntary Compliance Program, as currently operated, applies only to delinquent and non-filers. PWBA anticipates that applicants under the VFC Program will need only to amend their previously filed Forms 5500 to the extent the prohibited transactions or improper valuations were not reported adequately. Accordingly, there is no need to merge the two programs. Nonetheless, if a plan has filing problems and transactions that could be corrected through the VFC Program, all of which need to be corrected, plan officials may wish to consider applying to both programs simultaneously.

Anonymous Presubmissions

Commenters suggested that the public would benefit from the ability of potentially liable parties to presubmit applications anonymously to PWBA prior to filing a formal application for relief under the Program. Certain commenters suggested that if the determination as to the type of transaction to be included in an application and the correction method to be used were negotiated on an anonymous basis, PWBA could negotiate the precise relief necessary without engaging in a settlement agreement within the meaning of section 502(l). PWBA does not believe that it is either practical or appropriate to amend the VFC Program to provide for a formal anonymous presubmission process. A formal process would result in duplicative effort and could be cumbersome to administer. In addition, PWBA believes that negotiation of the type of transaction and the appropriate correction could lead to a settlement within the meaning of section 502(l) even if the negotiations took place on an anonymous basis. PWBA notes that each regional PWBA office has a VFC Program Coordinator. Members of the public are free to contact the VFC Program Coordinator and discuss on an informal, hypothetical basis general issues regarding the scope of the Program, including the types of transactions appropriate for an application and the types of correction that would satisfy the Program.

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EXHIBIT 3 Adoption of Voluntary Fiduciary Correction Program [03/28/2002], Continued

Ability To Amend Application To Avoid Final Rejection

One commenter requested that the VFC Program expressly provide for amendment of applications. The commenter suggested that Plan Officials be given the opportunity to conduct their own compliance reviews after submitting a preliminary application outlining suspected but uncorrected breaches. The comment stated that such a procedure would enable fiduciaries to resolve known and undiscovered breaches during the compliance review. The commenter suggested that the Department defer any enforcement action pending its receipt of the final application. The commenter also suggested that the VFC Program provide that if the Department intended to reject an application, it provide notice to the applicant, the basis for rejection, and a deadline for correcting deficiencies. The Department believes a formal procedure for amendment of applications as proposed by the commenter is not necessary. The Department emphasizes that the VFC Program includes no limitations on amendment of applications provided such change does not result from negotiation with PWBA. Accordingly, PWBA does not believe it is necessary to amend the VFC Program to provide for a formal procedure. In its administration of the VFC Program, PWBA anticipates providing applicants sufficient opportunity, as the circumstances warrant, to correct defects.

Tolling Agreements

One commenter suggested that certain applicants might desire to enter into tolling agreements with PWBA. This commenter requested that tolling agreements be made part of the VFC Program. PWBA believes that only in rare situations would it be necessary to use tolling agreements in connection with the VFC Program. PWBA believes that in most situations, the transaction that is the subject of the application will be fully corrected in accordance with the VFC Program and there will be no extenuating circumstances that would warrant a tolling agreement with respect to the transaction or related transactions. However, in situations where an applicant believes that it will need additional time to complete an application or to file additional applications for related transactions, PWBA will consider entering into tolling agreements with the applicant. The mere fact that an applicant has entered into a tolling agreement with respect to a transaction or transactions ultimately corrected pursuant to a formal application under the VFC Program will not itself take the application out of the VFC Program and subject the applicant to the possibility of the imposition of section 502(l) penalties. PWBA does not believe, however, that it is necessary to amend the VFC Program formally to permit or require tolling agreements.

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EXHIBIT 3 Adoption of Voluntary Fiduciary Correction Program [03/28/2002], Continued

Whether Persons Other Than the Applicant Should Be Entitled to Relief Under the VFC Program

Various commenters expressed concern that the relief under the VFC Program was limited to the Program applicant and was not extended to all persons who might have participated in the breach. PWBA does not believe that it is appropriate to extend relief to persons who have not participated in the application process. The application process requires persons in a position to correct the breach to evaluate the transaction and correction and to attest under penalty of perjury as to the accuracy of the application, including whether the correction has been made in accordance with the VFC Program. PWBA notes that more than one party can submit an application. Thus, for example, if a plan sponsor, as the named fiduciary, decides to correct a transaction, and all the plan fiduciaries involved in the transaction join in the submission of the application, including executing the penalty of perjury statement, the relief provided under the VFC Program would extend to all the fiduciaries participating in the application. The Program has been amended to make clear that any number of Plan Officials may be applicants who sign the penalty of perjury statement.

Penalty of Perjury Statement

PWBA received numerous comments that the penalty of perjury statement (Section 6(g)) needed clarification. Several comments noted that the penalty of perjury statement appears to be broader than the eligibility standards (Section 4, VFC Program Eligibility). One commenter questioned why both a plan fiduciary with knowledge of the transaction and the applicant's authorized representative (if any) must sign and date the statement. The commenter represented that the transaction at issue would typically be beyond the personal knowledge of the representative. PWBA has decided to retain the language of the original penalty of perjury statement. The penalty of perjury statement, eligibility provisions, and PWBA's reservation of the right to reject an application when warranted by facts and circumstances are all intended to help the potential applicant evaluate whether participation in the VFC Program is appropriate. PWBA believes these provisions are necessary to limit its review to the application only and to avoid follow-up investigations that could render the Program less efficient and focused. PWBA believes the review and signature of the authorized representative is a necessary safeguard that presents an insignificant burden.

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EXHIBIT 3 Adoption of Voluntary Fiduciary Correction Program [03/28/2002], Continued

Scope of the Term ``Under Investigation''

PWBA received several comments requesting clarification of Section 3(b)(3) (Under Investigation) of the VFC Program. In response to the comments, PWBA is amending the definition of Under Investigation to clarify that the definition does not include work paper reviews initiated by PWBA's Office of Chief Accountant under authority of section 504(a) of ERISA. Although PWBA is not making any further amendments to the definition, PWBA also notes, by way of clarification, that a party is Under Investigation if it has received oral or written notification from PWBA of a PWBA investigation of the plan concerning any issue. However, a plan is not Under Investigation if PWBA staff have contacted a Plan Official or representative in connection with a participant complaint that does not relate to a transaction described in the VFC Program application.

Required Documentation Under the VFC Program

Commenters suggested that various types of documentation required by the VFC Program are unnecessary or overly burdensome. One commenter suggested that there is no reason to require the provision of a fidelity bond. Another commenter questioned the need to provide a copy of the entire plan document as part of the application and suggested that providing the relevant portion of the plan should be adequate. PWBA has determined to retain generally all of the documentation requirements of the VFC Program. The documentation is necessary for PWBA to evaluate fully the application and the transaction at issue. However, PWBA believes that streamlining the documentation requirements may encourage additional participation in the VFC Program. Accordingly, PWBA is eliminating the requirement in Section 6(e)(i) of the Interim VFC Program that applicants produce a copy of the fidelity bond. Instead, Section 6(e)(i) of the VFC Program now provides that applicants need only identify in their application the current fidelity bond that meets the requirements of section 412 of ERISA. In addition, the Program is amended to require only production of relevant portions of the plan with the initial application. There may be situations where PWBA will want to examine additional provisions of the plan when reviewing the application. Accordingly, the VFC Program now provides that as part of the application process, applicants may be required to produce the entire plan document on request.

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EXHIBIT 3 Adoption of Voluntary Fiduciary Correction Program [03/28/2002], Continued

Departmental Approval of Preventive Measures Taken by Applicants
Section 2(c)(2) (Effect of the VFC Program--No implied approval of other matters) states that a no action letter does not imply approval of steps that fiduciaries take to prevent recurrence of the breach described in an application and to ensure future compliance with Title I of ERISA. Appendix B (VFC Program Checklist) at item 12 asks whether the plan has implemented measures to ensure that the transactions specified in the application do not recur. Appendix B states that PWBA will not opine on the adequacy of these measures. One commenter requested that Plan Officials be given the opportunity to request and obtain PWBA's approval of preventive measures. PWBA believes such a procedure is beyond the scope of the VFC Program. A VFC Program application is an insufficient record upon which this type of opinion could be rendered, and PWBA designed the Program to avoid conducting additional inquiries.

Required Use of Independent and Expert Evaluations and Written Appraisals

Each of the Loan and Purchase, Sale, and Exchange corrections described in Section 7(b) and (c) of the Interim VFC Program requires that an independent party provide a specific determination or report. Additionally, the correction of Benefits and Plan Expenses transactions described in Sections 7(d) and (e) requires action by an independent appraiser and an estimator, respectively. Commenters generally represented that these requirements were unnecessary and impractical. One commenter suggested that PWBA clarify that ERISA does not mandate independent written appraisals prior to the sale of an asset that is not publicly traded. Another comment suggested that certification by the applicant or other alternative evidence of a fair market interest rate should suffice. The VFC Program's principle of independence derives in part from PWBA's prohibited transaction exemption program. PWBA believes the requirement for a neutral, qualified independent party is an established and proper safeguard. The unilateral nature of PWBA's application review also compels the requirement of an independent judgment. An objective of the Program is that PWBA need not audit the circumstances of the transaction and its correction. The VFC Program is designed to provide a record free of any appearance of self-dealing or imprudence in the correction of transactions. Accordingly, PWBA has decided not to amend the requirements for the use of independent and expert evaluations and appraisals.

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EXHIBIT 3 Adoption of Voluntary Fiduciary Correction Program [03/28/2002], Continued

The Revised VFC Program

The VFC Program as adopted here retains the same basic structure as the Interim VFC Program, while adding two new transactions. The effect of the VFC Program, the eligibility requirements, and the application procedures are unchanged. As discussed in more detail above in the responses to specific public comments, the major changes to the Program are the proposal to provide relief from some excise taxes associated with transactions that can be corrected under the Program and the elimination of the requirement of notice to participants, as described in Section 5(e) of the Interim VFC Program. As stated previously, where the applicant is eligible for and elects to take advantage of the excise tax relief available under the Class Exemption, the separate notice requirements of the Class Exemption must be met. The documentation requirements have been simplified to permit applicants to provide a statement that they have a fidelity bond, rather than provide a copy of the bond itself. Additionally, applicants need only submit relevant portions of the applicable plan documents with the application, rather than the entire plan document.

Executive Order 12866

Under Executive Order 12866, the Department must determine whether a regulatory action is ``significant'' and therefore subject to the requirements of the Executive Order and subject to review by the Office of Management and Budget (OMB). Under section 3(f), the order defines a ``significant regulatory action'' as an action that is likely to result in a rule (1) having an annual effect on the economy of $100 million or more, or adversely and materially affecting a sector of the economy, productivity, competition, jobs, the environment, public health or safety, or State, local or tribal governments or communities (also referred to as ``economically significant''); (2) creating serious inconsistency or otherwise interfering with an action taken or planned by another agency; (3) materially altering the budgetary impacts of entitlement grants, user fees, or loan programs or the rights and obligations of recipients thereof; or (4) raising novel legal or policy issues arising out of legal mandates, the President's priorities, or the principles set forth in the Executive Order.

Pursuant to the terms of the Executive Order, it has been determined that this action would create a novel method for accomplishing compliance while reducing regulatory burdens and making effective use of federal resources. As such, this notice is consistent with the principles of the Executive Order. Therefore, this action is ``significant'' and subject to OMB review under section 3(f)(4) of the Executive Order.

In the Department's view, the benefits of the VFC Program will substantially outweigh its costs, because participation is voluntary, the administrative cost of correcting a potential fiduciary breach through voluntary participation in the Program is lower than the cost of a correction resulting from investigation and litigation, and the value and security of the assets of plans participating in the Program will be increased.

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EXHIBIT 3 Adoption of Voluntary Fiduciary Correction Program [03/28/2002], Continued

No costs are imposed by the VFC Program unless Plan Officials choose to avail themselves of the opportunity to correct a potential fiduciary breach under the terms of the Program. Because the decision to participate in the VFC Program is made by the relevant Plan Officials, participation is expected to occur only when the projected benefit outweighs the anticipated cost for the plan. The costs of electing to correct potential breaches of fiduciary responsibility under the terms of the VFC Program are expected to arise from the requirement for those participating in the VFC Program to obtain fair market value determinations, computations of losses or profits on the use of plan assets, the administrative costs of supplemental distributions, recomputations of account balances, transaction costs for disposal of assets, and the description and documentation of the correction for purposes of the application to the Department.

The value of assets or losses restored to employee benefit plans as a result of Plan Officials' participation in the VFC Program is viewed as a transfer from a fiduciary or other party in interest to the participants and beneficiaries of the plan. Plan Officials may not transfer the costs of compliance with the terms of this VFC Program to participants and beneficiaries.

The principal benefit of this VFC Program accrues to participants and beneficiaries through restoration of losses to the plan or reversal of impermissible transactions involving the assets of the plan, resulting in greater security of their plan assets. Benefits also accrue to plan fiduciaries through both risk reduction and the savings of civil penalties that would otherwise be payable on the amount of assets recovered by plans following a civil investigation or litigation. Where the Department determines that it will take no civil enforcement action and recommend no further legal action in response to a completed application under the VFC Program, the fiduciary is relieved of potential demands on its resources that might be imposed by a civil investigation and any subsequent litigation.

The VFC Program also allows the Department to encourage compliance with Part 4 of Title I of ERISA while making even more effective use of its limited enforcement resources. The Department believes that the correction of violations through the VFC Program is less costly than correction through active intervention, and that VFC Program applicants have a high likelihood of accomplishing an appropriate correction of a potential violation. To the extent that Plan Officials who wish to correct potential violations do so voluntarily and appropriately, the Department may direct its resources toward other areas where active intervention is more likely to be necessary.

More generally, publication of the specific examples of transactions which may violate ERISA and the activities required to correct those violations will serve to better inform plan fiduciaries and assist them in satisfying their fiduciary obligations in future transactions involving plan assets.

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EXHIBIT 3 Adoption of Voluntary Fiduciary Correction Program [03/28/2002], Continued

Under the Interim VFC Program, the total benefit to participants and beneficiaries is estimated at approximately $80 million, while the benefit to Plan Officials, to the extent it can be quantified, is estimated at $5.4 million. The Department originally estimated the cost of the Interim VFC Program for the Plan Officials who chose to participate at $1.9 million. Because the Department has amended the VFC Program by streamlining documentation requirements, the overall benefits and costs of the Program as adopted vary from those proposed in the Interim VFC Program only to the extent that the estimated cost for applying to the Program for 700 Plan Officials has been reduced to $1.8 million as a result of the modification in the documentation requirements. Under the Interim VFC Program, initial estimates of costs and benefits were based on the upper bound of the number of Plan Officials that might avail themselves of the Program based on the transactions eligible for correction. Because the actual number of Plan Officials that have taken advantage of the program, averaged over a nine-month period, has not contradicted the original estimates, the Department continues to believe that 700 Plan Officials remains a reasonable estimate of the number of applicants that will avail themselves of the VFC Program. The number of Program participants during the initial months of the Program has been lower than originally projected. However, the addition of a transaction to the permanent Program, the availability of the related exemption, and the elimination of the notice requirement except for that in the related exemption, is expected to increase participation.

Finally, these figures do not include an estimate of the potential benefit to Plan Officials of the reduced risk of investigation and litigation, or the benefit to the Department, to participants and beneficiaries, and to the public in general of realizing efficiencies in the use of enforcement resources because these elements are not readily quantifiable. Because this VFC Program is voluntary, the Department assumes that Plan Officials will in no event make use of the VFC Program unless the projected benefit outweighs the estimated cost of participation.

A discussion of the elements of the costs and benefits of this VFC Program and estimates of their magnitude where they can be specifically quantified follows. Based on the Department's previous experience with the Pension Payback Program, in which approximately 0.1 percent of plans that permitted employee contributions elected to participate during the six-month period when the Pension Payback Program was in effect, the Department projects that Plan Officials of approximately 700 plans will apply for and use the VFC Program. The Department expects a similar rate of participation among the approximately 200,000 plans that currently permit employee contributions. However, it assumes the participation by Plan Officials of 200 plans will occur over an annual period in the absence of the six-month time limitation included in the Pension Payback Program. Because the VFC Program permits correction of several other types of transactions in addition to the repayment of delinquent employee contributions, the Department has assumed that the annual rate of participation in the VFC Program by Plan Officials of plans other than those which permit employee contributions will be comparable to the 0.1 per cent assumed for those which permit employee contributions, resulting in participation by Plan Officials of about 500 additional plans, and total participation of 700 plans.

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EXHIBIT 3 Adoption of Voluntary Fiduciary Correction Program [03/28/2002], Continued

The Department views this estimate as an upper bound; actual participation may be somewhat smaller depending on the cost effectiveness of correcting the actual transactions involved, the complexity of the legal and factual issues involved in a given transaction, and the degree of similarity between a specific transaction representing a breach of fiduciary responsibility and a transaction and correction described by the terms of the VFC Program. The Department recognizes that Plan Officials may not view the VFC Program as offering a cost-effective means of correcting all potential violations.

The Department also estimates that $80 million, or an average of $114,300 per plan, will be recovered by plans annually as a result of participation in the VFC Program. Based on its enforcement experience, the Department estimates that about 70 per cent of this total, or $56 million, will consist of restored principal and earnings losses, and restored profits on the use of plan assets by fiduciaries or parties in interest. The total estimated recovery represents the midpoint between the average monetary recovery (excluding assets recovered through litigation) per plan that resulted from civil investigations completed by the Department in the year ended September 30, 1998, and the average per plan monetary recovery which arose from the Pension Payback Program, as applied to the 700 plans assumed to elect to participate in the VFC Program. The Department believes this estimate is reasonable in light of the range of transactions which may be corrected under the VFC Program. It is estimated that approximately 88,000 participants, or an average of 126 participants per plan, will be affected annually by corrections under the VFC Program.

Based on its recent experience with the collection of civil penalties under section 502(l), the Department estimates that Plan Officials will be relieved of approximately $5.4 million in civil penalties as a result of correction of transactions through the VFC Program. This estimate is based on the 700 plans assumed to participate, and the average 502(l) penalty actually collected per plan subject to the penalty in the last two fiscal years. Actual collections take into account the offset of any excise tax payable as a result of a violation of section 4975 of the Code. Relief from section 4975 excise taxes under the Code is available to Plan Officials under the newly proposed Class Exemption to Permit Certain Transactions identified in the Voluntary Fiduciary Correction Program, also published simultaneously in this issue of the Federal Register (Application No. D-10933).

The costs for Plan Officials to participate in the VFC Program arise from a range of possible required activities depending on the nature of the transaction to be corrected, including evaluation by Plan Officials and their professionals of the need and usefulness of participation in the VFC Program, obtaining market value determinations, executing asset transactions, adjusting account balances and benefit distributions, documenting the correction, and completing and mailing the application to participate in the Program.

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EXHIBIT 3 Adoption of Voluntary Fiduciary Correction Program [03/28/2002], Continued

The Department anticipates that Plan Officials will in most cases seek the services of a professional (typically an attorney, accountant, or professional administrator) to conduct the applicable activities, although the resources of Plan Officials are expected to be needed as well to gather information, and prepare, sign, and photocopy the application. It is estimated that the entire correction will require approximately 39 hours to complete, including 8 hours of the Plan Official's time, and 31 hours of a professional's time.

At the assumed rate of participation, the total cost of these activities is estimated to amount to $1.8 million (or an average of $2,600 per Plan Official), at an average cost of $57 per hour for work performed in house by Plan Officials and their employees, and a rate of $70 per hour for purchased services. This estimate also includes application materials and mailing costs.

Paperwork Reduction Act

At the time of publication of the Interim VFC Program in the Federal Register (65 FR 14164, Mar. 15, 2000), the Department submitted to OMB the information collection request (ICR) included in the Interim VFC Program using emergency procedures for review and clearance in accordance with the Paperwork Reduction Act of 1995 (PRA 95) (44 U.S.C. Chapter 35). Although the Department requested emergency review of the ICR by April 14, 2000, and OMB granted approval of the ICR through September 30, 2000, the Department continued to receive comments until May 15, 2000. The OMB number assigned to the ICR is 1210-0118. The Department subsequently applied for and was granted approval by OMB for an extension of the information collection request. The current OMB approval for this ICR will expire on November 30, 2003. Based on comments received from the public after the Notice in the Federal Register and additional consideration by the Department, modifications in the documentation and notification requirements were made to the Interim VFC Program. No comments were received in response to the Department's solicitation of comments concerning the ICR included in the Interim VFC Program. The changes in the hour and cost burdens reflected below are therefore the result of changes made by the Department to the VFC Program as adopted.

The VFC Program permits Plan Officials voluntarily to correct certain potential violations of Part 4 of Title I of ERISA, resulting in the receipt of a ``no action'' letter from the Department signifying that the applicant had been relieved of the possibility of civil investigation for that breach and/or civil action by the Secretary with respect to that breach, as well as the imposition of civil penalties under section 502(l) of ERISA. Comments received, however, requested that the Department also consider granting relief from the excise taxes imposed on prohibited transactions under section 4975 of the Code because the taxes were considered by Plan Officials to be a disincentive for participation in the VFC Program. In response, the Department is publishing simultaneously the proposed Class Exemption.

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EXHIBIT 3 Adoption of Voluntary Fiduciary Correction Program [03/28/2002], Continued

Under the Interim VFC Program, notification to interested persons of the application and correction of the eligible transaction was considered a condition for obtaining a ``no action'' letter. A number of commenters, however, observed that a notice of correction was not generally required by the Department in other circumstances where corrections have occurred and that notification was therefore unnecessary and burdensome. While the Department agreed to remove the notice requirement from the VFC Program, the Department also determined that where a Plan Official intended to seek relief from section 4975 of the Code, interested persons should be made aware of the material facts of the eligible transaction and the resulting correction. Therefore, under the VFC Program as adopted, the notice requirement has been eliminated as a part of the application process; however, a notice requirement has been included among the conditions for relief under the Class Exemption. For purposes of the PRA, the ICR previously described under the Interim VFC Program has been revised to indicate that notification is now a requirement under the Class Exemption rather than under the VFC Program as implemented on a permanent basis. Because the Class Exemption is only used in connection with the VFC Program, the Class Exemption also published simultaneously herewith is treated for purposes of the PRA as a modification of the information collection requirements of the VFC Program.

Based on additional observations received from commenters, the Department has also reduced the documentation required to be included with an application. Proof of bonding, formerly indicated by including a copy of the bond with the application, has been simplified by permitting a Plan Official to simply state in the application that the plan has a current fidelity bond that meets the requirements of section 412 of ERISA. Finally, the Program has been amended to require only production of relevant portions of the employee benefit plan, instead of a copy of the entire plan, with the initial application.

The ICR included in the VFC Program as adopted requires a Plan Official to describe the correction of the potential breach of fiduciary duty and to provide supporting documentation with respect to the correction. The type of supporting documentation will vary with the nature of the transaction involved, but is described in this VFC Program in as specific a manner as feasible. The Plan Official is also required to complete an application, which includes identification of the employee benefit plan and the Plan Official, or representative, relevant plan documents, a statement under penalty of perjury, and signature. Under certain circumstances, for instance if the correction under the Program involves an adjustment of account balances or supplemental distributions for participants or beneficiaries, the plan is expected to explain the basis for the adjustment or distribution. Because plans regularly report to participants or beneficiaries on changes in their account balance, the Department has not attributed an additional cost for disseminating this information. The information submitted to the Department will permit the Department to verify the correction of potential fiduciary breaches and restoration of losses, to evaluate the adequacy of actions taken by a Plan Official pursuant to the VFC Program, and to determine whether further action is necessary to protect the rights of participants and beneficiaries.

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EXHIBIT 3 Adoption of Voluntary Fiduciary Correction Program [03/28/2002], Continued

It is estimated that Plan Officials of 700 employee benefit plans will avail themselves of the opportunity to correct potential violations pursuant to the VFC Program. The Department estimates that approximately 8 hours of a Plan Official's time will be required to assemble documents and complete and sign the application to participate in the VFC Program. For 700 Plan Officials, the total hour burden is 5,600 hours. At a cost of $57 per hour for a financial manager's time, the administrator most likely to compile the necessary documents, the cost of the hour burden is $319,200.

It is further assumed that evaluation, correction, and documentation of transactions under the VFC Program will require approximately 31 hours, and that Plan Officials will generally elect to hire service providers to complete this work. The Department originally allotted six hours of a service provider's time for the completion of work attributed to the information collection. This included preparing descriptions and documentation, copying relevant supporting statements, and completing the application. Based on comments received on the Interim VFC Program, the Department has reduced the amount of supporting documentation required for the application process (i.e., requiring that only relevant parts of plan documents be submitted and acknowledging that a statement fidelity bonding is sufficient to replace a copy of the bond) and removed the notice requirement from the VFC Program as adopted and included it with the proposed exemption. Because of the changes in document production and notification, the Department has reduced by one hour the number of hours expected to be associated with information collection by service providers under the Program as adopted. Based on the reduction from six to five hours for purchased services, and at an assumed hourly rate of $70 per hour, the total estimated cost to 700 Plan Officials is $246,400. This includes an allowance of $2 per application for materials and mailing costs.

Agency: Pension and Welfare Benefits Administration, Department of Labor.
Title: Voluntary Fiduciary Correction Program.
OMB Number: 1210-0118.
Affected Public: Business or other for-profit; Not-for-profit institutions.
Frequency of Response: On occasion.
Total Respondents: 700.
Total Responses: 700.
Estimated Burden Hours: 5,600 for existing ICR.
Estimated Annual Costs (Operating and Maintenance): $246,400.

Persons are not required to respond to the collection of information unless it displays a currently valid OMB control number.

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EXHIBIT 3 Adoption of Voluntary Fiduciary Correction Program [03/28/2002], Continued

Regulatory Flexibility Act

This document reflects an enforcement policy of the Department and is not being issued as a general notice of proposed rulemaking. Therefore, the Regulatory Flexibility Act (5 U.S.C. 601 et seq.) (RFA) does not apply. However, PWBA considered the potential costs and benefits of this action for small plans and their Plan Officials in developing the VFC Program.

PWBA generally considers a small entity to be an employee benefit plan with fewer than 100 participants. The basis of this definition is found in section 104(a)(2) of ERISA, which permits the Secretary of Labor to prescribe simplified annual reports for pension plans, which cover fewer than 100 participants. However, because the VFC Program specifically prohibits the cost of participation from being borne by the plan and participants, this Program will impose no costs on the plans, which realize the benefits of the correction of potential violations. Costs will be borne instead by the Plan Officials of an estimated 700-employee benefit plans each year. Plan Officials may include both individual fiduciaries, plan sponsors, or parties in interest, and businesses in their roles as fiduciaries, plan sponsors, or parties in interest.

Although the number of Plan Officials of small plans that will elect to avail themselves of the opportunity to correct potential breaches of fiduciary duty under the terms of the VFC Program is not known, the potential costs and benefits to each Plan Official are summarized below, on the basis of the assumption that each of the participating Plan Officials will itself be a small entity.

Participation in the VFC Program is entirely voluntary, and as such, it is assumed that Plan Officials will elect to participate only when the potential benefits to a Plan Official are expected to exceed the cost of participation. Benefits may include the reduction of exposure to the risk of investigation and subsequent litigation, the potential cost of which cannot be specifically quantified, and the saving of penalties under section 502(l) of ERISA which would otherwise be payable on amounts required to be restored to plans by fiduciaries pursuant to a settlement agreement with the Department or court order.

As described in detail above, to the extent that the per small Plan Official costs and benefits of participation in the VFC Program can be quantified, assuming all participating Plan Officials are small entities, administrative costs of participation are estimated to amount to an average of $2,600 per Plan Official, while savings of section 502(l) penalties are estimated at $7,754 per Plan Official. While the average value of assets estimated to be restored to a plan as a result of participation in the VFC Program ($114,300 per plan) may be viewed as an expense by Plan Officials, the Department believes that this expense arises from a previously occurring breach of fiduciary duty rather than from participation in the VFC Program. The fiduciary's potential liability for a breach of fiduciary duty and the cost of remedial relief are expected to be comparable regardless of whether a violation is corrected under the terms of the VFC Program or as a result of an investigation and any subsequent litigation.

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EXHIBIT 3 Adoption of Voluntary Fiduciary Correction Program [03/28/2002], Continued

On this basis, Plan Officials of small plans electing to correct previously occurring fiduciary breaches through participation in the VFC Program are expected to derive a net benefit, even without consideration of the potential savings associated with the reduction of risk of exposure of its resources in connection with an investigation or litigation. Because penalties and additional resource demands are often relatively more burdensome for small entities than large, the Department views the VFC Program as offering a flexible and economically advantageous alternative to currently available methods of correcting potential breaches of fiduciary duty.

Unfunded Mandates Reform Act

For purposes of the Unfunded Mandates Reform Act of 1995 (Pub. L. 104-4), as well as Executive Order 12875, this regulatory action does not include any Federal mandate that may result in expenditures by State, local, or tribal governments, and will not impose an annual burden of $100 million or more on the private sector.

Federalism

The Department has reviewed this rule in accordance with Executive Order 13132 regarding Federalism. The order requires that agencies, to the extent possible, refrain from limiting state policy options, consult with states prior to taking any action, which would restrict state policy options or impose substantial direct compliance costs on state and local governments, and take such action only when there is clear constitutional authority and the presence of a problem of national significance. Since this rule does not limit state policy options or impose costs on state and local governments, it does not have federalism implications, and thus Executive Order 13132 does not require a certification that the VFC Program complies with the order.

Congressional Review Act

The VFC Program is subject to the provisions of the Congressional Review Act (5 U.S.C. 801 et seq.) and will be transmitted to Congress and the Controller General for review. The program is not a ``major rule'' as that term is defined in 5 U.S.C. 804 because it is not likely to result in (1) an annual effect on the economy of $100 million or more; (2) a major increase in costs or prices for consumers, individual industries, or federal, State, or local government agencies, or geographic regions; or (3) significant adverse effects on competition, employment, investment, productivity, innovation, or on the ability of the United States-based enterprises to compete with foreign-based enterprises in domestic or export markets.

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EXHIBIT 3 Adoption of Voluntary Fiduciary Correction Program [03/28/2002], Continued

Voluntary Fiduciary Correction Program

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EXHIBIT 3 Adoption of Voluntary Fiduciary Correction Program [03/28/2002], Continued

Appendix A. Sample VFC Program No Action Letter
Appendix B. VFC Program Checklist
Appendix C. List of PWBA Regional Offices
Section 1. Purpose and Overview of the VFC Program

The purpose of the VFC Program is to protect the financial security of workers by encouraging identification and correction of transactions that violate Part 4 of Title I of ERISA. Part 4 of Title I of ERISA sets out the responsibilities of employee benefit plan fiduciaries. Section 409 of ERISA provides that a fiduciary who breaches any of these responsibilities shall be personally liable to make good to the plan any losses to the plan resulting from each breach and to restore to the plan any profits the fiduciary made through the use of the plan's assets. Section 405 of ERISA provides that a fiduciary may be liable, under certain circumstances, for a co-fiduciary's breach of his or her fiduciary responsibilities. In addition, under certain circumstances, there may be liability for knowing participation in a fiduciary breach. In order to assist all affected persons in understanding the requirements of ERISA and meeting their legal responsibilities, PWBA is providing guidance on what constitutes adequate correction under Title I of ERISA for the breaches described in this Program.

Section 2. Effect of the VFC Program

(a) In general. PWBA generally will issue to the applicant a no action letter \4\ with respect to a breach identified in the application if the eligibility requirements of Section 4 are satisfied and a Plan Official corrects a breach, as defined in Section 3, in accordance with the requirements of Sections 5, 6 and 7. Pursuant to the no action letter it issues, PWBA will not initiate a civil investigation under Title I of ERISA regarding the applicant's responsibility for any transaction described in the no action letter, or assess a civil penalty under section 502(l) of ERISA on the correction amount paid to the plan or its participants.

\4\ See Appendix A.

(b) Verification. PWBA reserves the right to conduct an investigation at any time to determine (1) the truthfulness and completeness of the factual statements set forth in the application and (2) that the corrective action was, in fact, taken.

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EXHIBIT 3 Adoption of Voluntary Fiduciary Correction Program [03/28/2002], Continued

(c) Limits on the effect of the VFC Program. (1) In general. Any no action letter issued under the VFC Program is limited to the breach and applicants identified therein. Moreover, the method of calculating the correction amount described in this Program is only intended to correct the specific breach described in the application. Methods of calculating losses other than, or in addition to, those set forth in the Program may be more appropriate, depending on the facts and circumstances, if the transaction violates provisions of ERISA other than those that can be corrected under the Program. In this regard, the Program assumes, for example, that the transaction is otherwise an appropriate investment decision for the plan.

If a transaction gave rise to violations not addressed in the Program, such as imprudence not addressed in the Program or a failure to diversify plan assets, the relief afforded by the Program would not extend to such additional violations.

(2) No implied approval of other matters. A no action letter does not imply Departmental approval of matters not included therein, including steps that the fiduciaries take to prevent recurrence of the breach described in the application and to ensure the plan's future compliance with Title I of ERISA.

(3) Material misrepresentation. Any no action letter issued under the VFC Program is conditioned on the truthfulness, completeness and accuracy of the statements made in the application and of any subsequent oral and written statements or submissions. Any material misrepresentations or omissions will void the no action letter, retroactive to the date that the letter was issued by PWBA, with respect to the transaction that was materially misrepresented.

(4) Applicant fails to satisfy terms of the VFC Program. If an application fails to satisfy the terms of the VFC Program, as determined by PWBA, PWBA reserves the right to investigate and take any other action with respect to the transaction and/or plan that is the subject of the application, including refusing to issue a no action letter.

(5) Criminal investigations not precluded. Compliance with the terms of the VFC Program will not preclude:

(i) PWBA or any other governmental agency from conducting a criminal investigation of the transaction identified in the application;

(ii) PWBA's assistance to such other agency; or

(iii) PWBA making the appropriate referrals of criminal violations as required by section 506(b) of ERISA.\5\

\5\ Section 506(b) provides that the Secretary of Labor shall have the responsibility and authority to detect and investigate and refer, where appropriate, civil and criminal violations related to the provisions of Title I of ERISA and other related Federal laws, including the detection, investigation, and appropriate referrals of related violations of Title 18 of the United States Code.

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EXHIBIT 3 Adoption of Voluntary Fiduciary Correction Program [03/28/2002], Continued

(6) Other actions not precluded. Compliance with the terms of the VFC Program will not preclude PWBA from taking any of the following actions:
(i) Seeking removal from positions of responsibility with respect to a plan or other non-monetary injunctive relief against any person responsible for the transaction at issue;
(ii) referring information regarding the transaction to the IRS as required by section 3003(c) of ERISA; \6\ or

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\6\ Section 3003(c) provides that, whenever the Secretary of Labor obtains information indicating that a party in interest or disqualified person is violating section 406 of ERISA, she shall transmit such information to the Secretary of the Treasury.

(iii) imposing civil penalties under section 502(c)(2) of ERISA based on the failure or refusal to file a timely, complete and accurate annual report Form 5500. Applicants should be aware that amended annual
report filings may be required if possible breaches of ERISA have been identified, or if action is taken to correct possible breaches in accordance with the VFC Program.
(7) Not binding on others. The issuance of a no action letter does not affect the ability of any other government agency, or any other person, to enforce any rights or carry out any authority they may have, with respect to matters described in the no action letter.
(8) Example. A plan fiduciary causes the plan to purchase real estate from the plan sponsor under circumstances to which no prohibited transaction exemption applies. In connection with this transaction, the purchase causes the plan assets to be no longer diversified, in violation of ERISA section 404(a)(1)(C). If the application reflects full compliance with the requirements of the Program, the Department's no action letter would apply to the violation of ERISA section 406(a)(1)(A), but would not apply to the violation of section 404(a)(1)(C).
(d) Correction. The correction criteria listed in the VFC Program represent PWBA enforcement policy and are provided for informational purposes to the public, but are not intended to confer enforceable rights on any person who purports to correct a violation. Applicants are advised that the term ``correction'' as used in the VFC Program is not necessarily the same as ``correction'' pursuant to section 4975 of the Code.\7\ Correction may not be achieved under the Program by engaging in a new prohibited transaction.

\7\ See section 4975(f)(5) of the Internal Revenue Code (IRC); section 141.4975-13 of the temporary Treasury Regulations and section 53.4941(e)-1(c) of the Treasury Regulations. The Internal Revenue Service has indicated that except in those instances where the fiduciary breach or its correction result in a tax abuse situation or a plan qualification failure, a correction under this Program generally will be acceptable under the Internal Revenue Code.

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EXHIBIT 3 Adoption of Voluntary Fiduciary Correction Program [03/28/2002], Continued

(e) PWBA's authority to investigate. PWBA reserves the right to conduct an investigation and take any other enforcement action relating to the transaction identified in a VFC Program application in certain circumstances, such as prejudice to the Department that may be caused by the expiration of the statute of limitations period, material misrepresentations, or significant harm to the plan or its participants that is not cured by the correction provided under the VFC Program. PWBA may also conduct a civil investigation and take any other enforcement action relating to matters not covered by the VFC Program application or relating to other plans sponsored by the same plan sponsor, while a VFC Program application involving the plan or the plan sponsor is pending.

(f) Confidentiality. PWBA will maintain the confidentiality of any documents submitted under the VFC Program, to the extent permitted by law. However, as noted in (c)(5) and (6) of this section, PWBA has an obligation to make referrals to the IRS and to refer to other agencies evidence of criminality and other information for law enforcement purposes.

Section 3. Definitions

(a) The terms used in this document have the same meaning as provided in section 3 of ERISA, 29 U.S.C. section 1002, unless separately defined herein.

(b) The following definitions apply for purposes of the VFC Program:

(1) Breach. The term ``Breach'' means any transaction which is or may be a breach of the fiduciary responsibilities contained in Part 4 of Title I of ERISA.

(2) Plan Official. The term ``Plan Official'' means a plan fiduciary, plan sponsor, party in interest with respect to a plan, or other person who is in a position to correct a Breach.

(3) Under Investigation. The term ``Under Investigation'' means a plan or person that is being investigated pursuant to ERISA section 504(a) or any criminal statute involving a transaction which affects an employee benefit plan. A plan that is Under Investigation by PWBA includes any plan for which a Plan Official, or a plan representative, has received oral or written notification from PWBA of a PWBA investigation of the plan. A plan is not considered to be Under Investigation by PWBA merely because PWBA staff have contacted a Plan Official or representative in connection with a participant complaint, unless the participant complaint concerns the transaction described in the application. A plan also is not considered to be Under Investigation where it is undergoing a work paper review by PWBA's Office of the Chief Accountant under the authority of ERISA section 504(a).

Section 4. VFC Program Eligibility

Eligibility for the VFC Program is conditioned on the following:

(a) Neither the plan nor the applicant is Under Investigation.

(b) The application contains no evidence of potential criminal violations as determined by PWBA.

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EXHIBIT 3 Adoption of Voluntary Fiduciary Correction Program [03/28/2002], Continued

Section 5. General Rules for Acceptable Corrections

(a) Fair Market Value Determinations. Many corrections require that the current or fair market value of an asset be determined as of a particular date, usually either the date the plan originally acquired the asset or the date of the correction, or both. In order to be acceptable as part of a VFC Program correction, the valuation must meet the following conditions:

(1) If there is a generally recognized market for the property (e.g., the New York Stock Exchange), the fair market value of the asset is the average value of the asset on such market on the applicable date, unless the plan document specifies another objectively determined value (e.g., the closing price).

(2) If there is no generally recognized market for the asset, the fair market value of that asset must be determined in accordance with generally accepted appraisal standards by a qualified, independent appraiser and reflected in a written appraisal report signed by the appraiser.

(3) An appraiser is ``qualified'' if he or she has met the education, experience, and licensing requirements that are generally recognized for appraisal of the type of asset being appraised.

(4) An appraiser is ``independent'' if he or she is not one of the following, does not own or control any of the following, and is not owned or controlled by, or affiliated with, any of the following:

(i) The prior owner of the asset, if the asset was purchased by the plan;

(ii) The purchaser of the asset, if the asset was, or is now being sold, by the plan;

(iii) Any other owner of the asset, if the plan is not the sole owner;

(iv) A fiduciary of the plan;

(v) A party in interest with respect to the plan (except to the extent the appraiser becomes a party in interest when retained to perform this appraisal for the plan); or

(vi) The VFC Program applicant.

(b) Correction Amount. (1) In general. Many of the transactions described in the VFC Program result in a loss to the plan or a profit to some party to the transaction. Determining the amount of the loss to the plan requires calculating how much money the plan would have now if a particular transaction had not occurred. In general, the VFC Program requires the fiduciary or other Plan Official to restore to the employee benefit plan the Principal Amount, plus the greater of (i) Lost Earnings from the Loss Date to the Recovery Date or (ii) Restoration of Profits resulting from the use of the Principal Amount for the same period.

(2) Principal Amount. ``Principal Amount'' is the amount that would have been available to the plan for investment or distribution on the date of the Breach, had the Breach not occurred. What constitutes the Principal Amount is identified for each transaction set forth in Section 7 of the VFC Program. The generic term ``Principal Amount'' is the base on which Lost Earnings are calculated. The Principal Amount shall also include, where appropriate, any transaction costs, such as closing costs, associated with entering into the transaction that constitutes the Breach.

(3) Loss Date. ``Loss Date'' is the date that the plan lost the use of the Principal Amount.

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EXHIBIT 3 Adoption of Voluntary Fiduciary Correction Program [03/28/2002], Continued

(4) Recovery Date. ``Recovery Date'' is the date that the Principal Amount is restored to the plan.

(5) Lost Earnings. For purposes of the VFC Program, Lost Earnings to be restored to a plan is the greater of (i) the amount that otherwise would have been earned on the Principal Amount from the Loss Date to the Recovery Date had the Principal Amount been invested during such period in accordance with applicable plan provisions and Title I of ERISA, less actual net earnings or realized net appreciation (or, if applicable, plus any net loss to the plan as a result of the transaction), or (ii) the amount that would have been earned on the Principal Amount at an interest rate equal to the underpayment rate defined in section 6621(a)(2) of the Code, less actual net earnings or realized net appreciation (or, if applicable, plus any net loss to the plan as a result of the transaction). In addition, if the date on which the Lost Earnings is paid to the plan is a date after the Recovery Date, payment must include an additional amount that is the greater of (i) the amount that would have been earned by the plan on the Lost Earnings if it had been paid on the Recovery Date, or (ii) the amount that would have been earned on the Lost Earnings at an interest rate equal to the underpayment rate defined in section 6621(a)(2) of the Code. For a participant-directed defined contribution plan, the Lost Earnings to be restored to the plan is the amount that each participant would have earned on the Principal Amount from the Loss Date to the Recovery Date. However, for administrative convenience, the Lost Earnings amount for a participant-directed defined contribution plan may be calculated using the rate of return of the investment alternative that earned the highest rate of return among the designated broad range of investment alternatives available under the plan during the applicable period. For participants who have not made any participant directions, plan officials may use the plan's average of the rates of return earned by all the designated investment alternatives weighted by the portion of plan assets invested in these alternatives.

(6) Restoration of Profits. ``Restoration of Profits'' is the amount of profit made on the use of the Principal Amount, or the property purchased with the Principal Amount, by the fiduciary or party in interest who engaged in the Breach, or by a knowing participant in the Breach. If the Principal Amount was used for a specific purpose such that the actual profit can be determined, that actual profit must be calculated from the Loss Date to the Recovery Date and returned to the plan. If the Principal Amount was commingled with other funds so that the actual profit cannot be determined, the Restoration of Profits will be calculated as interest on the Principal Amount at an interest rate equal to the underpayment rate defined in section 6621(a)(2) of the Code. In addition, if the date on which the Restoration of Profits is paid to the plan is a date after the Recovery Date, payment must include an additional amount that is the greater of (i) the amount that would have been earned by the plan on the Restoration of Profits if it had been paid on the Recovery Date, or (ii) the amount that would have been earned on the Restoration of Profits at an interest rate equal to the underpayment rate defined in section 6621(a)(2) of the Code.

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EXHIBIT 3 Adoption of Voluntary Fiduciary Correction Program [03/28/2002], Continued

(7) The principles of this paragraph (b) are illustrated by the following examples:
Example 1. An employer who sponsors a plan with a qualified cash or deferred arrangement within the meaning of section 401(k)(2) of the Code (``401(k) plan'') could have reasonably paid participant contributions into the plan's trust account within two business days of each pay day. For this employer, the second business day after pay day was therefore the date on which the participant contributions become plan assets, because it is the earliest date on which this employer reasonably could have segregated the participant contributions from the employer's general assets.\8\ However, for the pay period ending January 31, a Monday, participant contributions totaling $10,000 were not deposited until March 2.

\8\ See 29 CFR 2510.3-102.

The Principal Amount is $10,000. The Loss Date is February 2, the date on which the participant contributions became plan assets and should have been deposited in the plan's trust account. The Recovery Date is March 2, the date that the participant contributions were deposited in the plan's trust account.

The 401(k) plan offers five investment alternatives representing a broad range of investment alternatives. During the month of February, one of the plan's mutual funds had a one percent return, including all reinvestment earnings. This was the highest return earned by any of the five investment alternatives in this period. The employer elects to use this rate of return for the loss calculations. Accordingly, the Lost Earnings amount is $100 ($10,000 multiplied by one percent).

The employer had the use of $10,000 of the 401(k) plan's assets between February 2 and March 2, while the participant contributions remained commingled with the employer's general assets. The employer's cost of funds (the actual profit from the use of the participant contributions) cannot readily be determined; therefore, the Restoration of Profits amount is calculated using the underpayment rate defined in Code section 6621(a)(2). Assuming the section 6621 rate was 9% (annualized yield for the relevant quarter), the Restoration of Profits amount is $75 ($10,000 multiplied by 9% per annum times one-twelfth of a year).

In this example, the Lost Earnings amount ($100) is greater than the Restoration of Profits amount ($75). Since the Principal Amount of $10,000 was paid to the plan on March 2, the total correction amount to be paid to the plan is the Lost Earnings of $100.

Assume further, in this example, that although the Principal Amount of $10,000 was paid to the plan on March 2, the Lost Earnings of $100 were not paid to the plan until a year later. The plan's annual yield for the highest earning fund was 12 percent. The employer elects to use the highest yielding fund for administrative convenience. Accordingly, an additional $12 ($100 multiplied by 12 percent--the annual yield), must be paid to the plan along with the $100 Lost Earnings amount.

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Example 2. On March 15, a plan's trustees authorized the purchase of 1,000 shares of stock. The plan paid $75 per share when the fair market value was $70 per share.\9\ The Principal Amount is $5,000 (1,000 shares multiplied by the $5 per share overpayment). The Loss Date is March 15, the date of the overpayment. The Recovery Date will be the date on which the fiduciary or other person repays to the plan the correction amount.

\9\ If a plan's fiduciaries authorized the purchase of a specific dollar amount of stock rather than the purchase of a specific number of shares, and the plan acquired fewer shares than it should have as a result of paying too much per share, the amount lost equals the number of additional shares that the plan should
have acquired, plus any appreciation, dividends, or stock splits associated with those additional shares.

Assume that the plan recoups the $5,000 overpayment a year after the original purchase. During this year, the plan's other investments earned 9%, including all reinvestment earnings. The Lost Earnings amount is $450 ($5,000 multiplied by 9% annual yield for one year). If the Restoration of Profit amount is less than $450, the total amount to be paid to the plan is $5,450 (the Principal Amount of $5,000 plus Lost Earnings of $450).

Example 3. Assume the same facts as in Example 2, except that the proceeds of the sale were used to make another investment, which yielded a 15% annual rate of return. The Restoration of Profits amount is $750 ($5,000 multiplied by 15% per annum times one year). In this example, the Restoration of Profits amount ($750) is greater than the Lost Earnings amount ($450). The total amount to be paid to the plan is $5,750 (the Principal Amount of $5,000 plus Restoration of Profits of $750).

Example 4. On April 20, a plan paid $6,000 in legal fees for legal services that the plan sponsor, not the plan, was obligated to pay. The Principal Amount is $6,000. The Loss Date is April 20, the date the plan improperly paid the plan sponsor's legal expenses. The Recovery Date will be the date on which the plan sponsor reimburses the plan $6,000. Assume that the plan sponsor reimburses the plan on October 20, six months after the Loss Date. During this period, the plan's investment earnings totaled five percent, including all reinvestment earnings. The Lost Earnings amount is $300 ($6,000 multiplied by five percent).

The plan sponsor had constructive use of $6,000 from April 20 until October 20. The plan sponsor's cost of funds (the actual profit from the use of the money) cannot readily be determined; therefore, the Restoration of Profits amount is calculated using the underpayment rate defined in Code section 6621(a)(2). Assuming the published section 6621 rate was 8% per annum for the duration of the period April 20 to October 20, the Restoration of Profits amount is $240 ($6,000 times 8% per annum multiplied by one-half).

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In this example, the Lost Earnings amount ($300) is greater than the Restoration of Profits amount ($240). The total amount to be paid to the plan is $6,300 (the Principal Amount of $6,000 plus Lost Earnings of $300).

(c) Costs of Correction. (1) The fiduciary, plan sponsor or other Plan Official, not the plan, shall pay the costs of correction.
(2) The costs of correction include, where appropriate, such expenses as closing costs, prepayment penalties, or sale or purchase costs associated with correcting the transaction.
(3) The principle of paragraph (c)(1) is illustrated in the following example and in (d) below:

Example: The plan fiduciaries did not obtain a required independent appraisal in connection with a transaction described in Section 7. In connection with correcting the transaction, the plan fiduciaries now propose to have the appraisal performed as of the date of purchase. The plan document permits the plan to pay reasonable and necessary expenses; the fiduciaries have objectively determined that the cost of the proposed appraisal is reasonable and is not more expensive than the cost of an appraisal contemporaneous with the purchase. The plan may therefore pay for this appraisal. However, the plan may not pay any costs associated with recalculating participant account balances to take into account the new valuation. There would be no need for these additional calculations or any increased appraisal cost if the plan's assets had been valued properly at the time of the purchase. Therefore, the cost of recalculating the plan participants' account balances is not a reasonable plan expense, but is part of the Costs of Correction.

(d) Distributions. Plans will have to make supplemental distributions to former employees, beneficiaries receiving benefits, or alternate payees, if the original distributions were too low because of the Breach. In these situations, the Plan Official or plan administrator must determine who received distributions from the plan during the time period affected by the Breach, recalculate the account balances, and determine the amount of the underpayment to each affected individual. The applicant must demonstrate proof of payment to participants and beneficiaries whose current location is known to the plan and/or applicant. For individuals whose location is unknown, applicants must demonstrate that they have segregated adequate funds to pay the missing individuals and that the applicant has commenced the process of locating the missing individuals using either the IRS and Social Security Administration locator services, or other comparable means. The costs of such efforts are part of the Costs of Correction.

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(e) De Minimus Exception. Where correction under the Program requires distributions in amounts less than $20 to former employees, their beneficiaries and alternate payees, who neither have account balances with, nor have a right to future benefits from the plan, and the applicant demonstrates in its submission that the cost of making the distribution to each such individual exceeds the amount of the payment to which such individual is entitled in connection with the correction of the transaction that is the subject of the application, the applicant need not make distributions to such individuals who would receive less than $20 each as part of the correction. However, the applicant must pay to the plan as a whole the total of such de minimus amounts not distributed to such individuals.

Example. Employer X sponsors Plan Y. Employer X submits an application under the VFC Program to correct a failure to forward timely participant contributions to the Plan Y. Employer X had paid the delinquent contributions six months late, but had not paid lost earnings on the delinquency. The correction under the VFC Program, therefore, required only payment of Lost Earnings for the six-month delinquency. During the six-month period 25 employees separated from service and rolled over their plan accounts to individual retirement accounts. The amount of lost earnings due to 20 of those former employees is less than $20, and Employer X demonstrates that the cost of making the distribution to those former employees is $27 per individual. Employer X need not make distributions to those 20 former employees. However, the total amount of distributions that would have been due to those former employees must be paid to Plan Y. The payment to Plan Y may be used for any purpose that payments or credits to Plan Y that are not allocated directly to participant accounts are used. Employer X must make distributions to the five former employees who are entitled to receive distributions of more than $20.

Section 6. Application Procedures

(a) In general. Each application must adhere to the requirements set forth below. Failure to do so may render the application invalid.

(b) Preparer. The application must be prepared by a Plan Official or his or her authorized representative (e.g., attorney, accountant, or other service provider). If a representative of the Plan Official is submitting the application, the application must include a statement signed by the Plan Official that the representative is authorized to represent the Plan Official.

(c) Contact person. Each application must include the name, address and telephone number of a contact person. The contact person must be familiar with the contents of the application, and have authority to respond to inquiries from PWBA.

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EXHIBIT 3 Adoption of Voluntary Fiduciary Correction Program [03/28/2002], Continued

(d) Detailed narrative. The applicant must provide to PWBA a detailed narrative describing the Breach and the corrective action. The narrative must include:

(i) a list of all persons materially involved in the Breach and its correction (e.g., fiduciaries, service providers, borrowers);

(ii) the EIN number and address of the plan sponsor and administrator;

(iii) the date the plan's most recent Form 5500 was filed;

(iv) an explanation of the Breach, including the date it occurred;

(v) an explanation of how the Breach was corrected, by whom and when; and

(vi) specific calculations demonstrating how Principal Amount and Lost Earnings or Restoration of Profits were computed and an explanation of why payment of Lost Earnings or Restoration of Profits
was chosen to correct the Breach.

(e) Supporting documentation. The applicant must also include:

(i) a statement that the plan has a current fidelity bond that meets the requirements of section 412 of ERISA and the name of the company providing the bond and the policy number;

(ii) copies of the relevant portions of the plan document and any other pertinent documents (such as the adoption agreement, trust agreement, or insurance contract);\10\

\10\ Applicants must supply complete copies of the plan documents and other pertinent documents if requested by PWBA during its review of the application.

(iii) documentation that supports the narrative description of the transaction and correction;

(iv) documentation establishing the Lost Earnings amount, including documentation of the return on the plan's other investments during the time period on which the Lost Earnings is calculated with respect to the transaction described in the VFC Program application;

(v) documentation establishing the amount of Restoration of Profits;

(vi) all documents described in Section 7 with respect to the transaction involved; and

(vii) proof of payment of Principal Amount and Lost Earnings or Restoration of Profits.

(5) Examples of supporting documentation. (i) Examples of documentation supporting the description of the transaction and correction are leases, appraisals, notes and loan documents, service provider contracts, invoices, settlement documents, deeds, perfected security interests, and amended annual reports.

(ii) Examples of acceptable proof of payment include copies of canceled checks, executed wire transfers, a signed, dated receipt from the recipient of funds transferred to the plan (such as a financial institution), and bank statements for the plan's account.

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EXHIBIT 3 Adoption of Voluntary Fiduciary Correction Program [03/28/2002], Continued

(g) Penalty of Perjury Statement. Each application must also include a Penalty of Perjury statement. The statement shall be signed and dated by a plan fiduciary with knowledge of the transaction that is the subject of the application and the authorized representative of the applicant, if any. In addition, all Plan Officials applying under the VFC Program must execute the Penalty of Perjury statement in order to be covered by the No Action Letter. The statement must accompany the application and any subsequent additions to the application. The statement shall read as follows:

I certify under penalty of perjury that I have reviewed this application and all supporting documents and that to the best of my belief the contents are true and complete and comply with all terms and conditions of the VFC Program. I further certify under penalty of perjury that at the date of this certification neither the Department nor any other Federal agency has informed me of an intention to investigate or examine the plan or otherwise made inquiry with respect to the transaction described in this application. I further certify under penalty of perjury that neither I nor any person acting under my supervision or control with respect to the operation of an ERISA-covered employee benefit plan:

(1) Is the subject of any criminal investigation or prosecution involving any offense against the United States;\11\

\11\ For purposes of this paragraph, an ``offense'' includes criminal activity for which the Department of Justice may seek civil injunctive relief under the Racketeer Influenced and Corrupt Organizations statute (18 U.S.C. 1964(b)). A ``subject'' is any individual or entity whose conduct is within the scope of any ongoing inquiry being conducted by a Federal investigator(s) who is authorized to investigate criminal offense against the United States.

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(2) Has been convicted of a criminal offense involving employee benefit plans at any time or any other offense involving financial misconduct which was punishable by imprisonment exceeding one year for which sentence was imposed during the preceding thirteen years or which resulted in actual imprisonment ending within the last thirteen years, nor has such person entered into a consent decree with the Department or been found by a court of competent jurisdiction to have violated any fiduciary responsibility provisions of ERISA during such period; or

(3) Has sought to assist or conceal the transaction described in this application by means of bribery, or graft payments to persons with fiduciary responsibility for this plan or with the knowing assistance of persons engaged in ongoing criminal activity.

(h) Checklist. The checklist in Appendix B must be completed, signed, and submitted with the application.

(i) Where to apply. The application shall be mailed to the appropriate regional PWBA office listed in Appendix C.

(j) Record keeping. The applicant must maintain copies of the application and any subsequent correspondence with PWBA for the period required by section 107 of ERISA.

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EXHIBIT 3 Adoption of Voluntary Fiduciary Correction Program [03/28/2002], Continued

Section 7. Description of Eligible Transactions and Corrections Under the VFC Program

PWBA has identified certain Breaches and methods of correction that are suitable for the VFC Program. Any Plan Official may correct a Breach listed in this Section in accordance with Section 5 and the applicable correction method. The correction methods set forth are strictly construed and are the only acceptable correction methods under the VFC Program for the transactions described in this Section. PWBA will not accept applications concerning correction of breaches not described in this Section.

A. Contributions

1. Delinquent Participant Contributions to Pension Plans

(a) Description of Transaction. An employer receives directly from participants, or withholds from employees' paychecks, certain amounts for contribution to a pension plan. Instead of forwarding the contributions for investment in accordance with the provisions of the plan and within the time frames described in the Department's regulation at 29 CFR 2510.3-102, the employer retains the contributions for a longer period of time.

(b) Correction of Transaction. (1) Unpaid Contributions. Pay to the plan the Principal Amount plus the greater of (i) Lost Earnings on the Principal Amount or (ii) Restoration of Profits resulting from the employer's use of the Principal Amount, as described in Section 5(b). The Principal Amount is the amount of the unpaid participant contributions and the Loss Date for each contribution is the earliest date on which the contributions reasonably could have been segregated from the employer's general assets. In no event shall the Loss Date be later than the applicable maximum time period described in 29 CFR 2510.3-102.

(2) Late Contributions. If participant contributions were remitted to the plan outside of the time period provided by the regulation, the only correction required is to pay to the plan the greater of (i) Lost Earnings or (ii) Restoration of Profits resulting from the employer's use of the Principal Amount as described in Section 5(b).

(3) Examples. The principles of this paragraph (b) are illustrated in the following examples:

Example 1. See Example 1 under Section 5(b).

Example 2. Employer X is a large national corporation, which sponsors a section 401(k) plan. X reasonably is able to segregate participant contributions no later than 10 business days after the end of the month in which participant contributions were withheld from employees' paychecks. For the pay period ending June 15, participant contributions totaling $900,000 were not deposited until August 14.

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The Principal Amount is $900,000. The Loss Date is July 14 (the tenth business day in July), the date on which the participant contributions became plan assets and should have been deposited in the plan's trust account. The Recovery Date is August 14, the date that the participant contributions were deposited in the plan's trust account.

The 401(k) plan offers eight investment alternatives with daily asset valuation. From July 14 through August 14, most of the plan participants experienced a decrease in their account balances due to a decline in the stock market; however, some participants had a net investment gain. The Code section 6621(a)(2) rate during this period was 8% (annual yield for all quarters) and was greater than the profit to the employer from the use of the funds during the pertinent time period.

For the participants whose account balances declined, the employer pays the Principal Amount plus the Restoration of Profits amount, calculated at 8% (annual yield). For the other participants, the employer pays the Principal Amount plus the higher of each participant's actual investment earnings between July 14 and August 14 or the Restoration of Profits amount calculated at 8%. Since the Principal Amount of $900,000 has already been paid to the plan, the correction amount to be paid to the plan is no less than the Restoration of Profits of $6,000 ($900,000 times 8% per annum multiplied by one-twelfth of a year).

(c) Documentation. In addition to the documentation required by Section 6, submit the following documents:

(1) For participant contributions received from participants, a copy of the accounting records which identify the date and amount of each contribution received;

(2) For participant contributions withheld from employees' paychecks, a copy of the payroll documents showing the date and amount of each withholding; and

(3) A statement from a Plan Official identifying the earliest date on which the participant contributions reasonably could have been segregated from the employer's general assets, along with the supporting documentation on which the Plan Official relied in reaching this conclusion.

2. Delinquent Participant Contributions to an Insured Welfare Plan

(a) Description of Transaction. Benefits are provided exclusively through insurance contracts issued by an insurance company or similar organization qualified to do business in any state or through a health maintenance organization (HMO) defined in section 1310(d) of the Public Heath Service Act, 42 U.S.C. 3000e-9(d). An employer receives directly from participants or withholds from employees' paychecks certain amounts that the employer forwards to an insurance provider for the purpose of providing group health or other welfare benefits. The employer fails to forward such amounts in accordance with the terms of the plan (including the provisions of any insurance contract) or the requirements of the Department's regulation at 29 CFR 2510.3-102. There are no instances in which claims have been denied under the plan, nor has there been any lapse in coverage, due to the failure to transmit participant contributions on a timely basis.

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EXHIBIT 3 Adoption of Voluntary Fiduciary Correction Program [03/28/2002], Continued

(b) Correction of Transaction. Pay to the insurance provider or HMO the Principal Amount, as well as any penalties, late fees or other charges necessary to prevent a lapse in coverage due to such failure. Any penalties, late fees or other such charges shall be paid by the employer and not from participant contributions.
(c) Documentation. In addition to the documentation required by Section 6, submit the following documents:
(1) For participant contributions received directly from participants, a copy of the accounting records which identify the date and amount of each contribution received;
(2) For participant contributions withheld from employees' paychecks, a copy of the payroll documents showing the date and amount of each withholding;
(3) A statement from a Plan Official identifying the earliest date on which the participant contributions reasonably could have been segregated from the employer's general assets, along with the supporting documentation on which the Plan Official relied in reaching this conclusion;
(4) Copies of the insurance contract or contracts for the group health or other welfare benefits for the plan;
(5) A statement from a Plan Official attesting that there are no instances in which claims have been denied under the plan for nonpayment, nor has there been any lapse in coverage; and
(6) A statement from a Plan Official attesting that any penalties, late fees or other such charges have been paid by the employer and not from participant contributions.

3. Delinquent Participant Contributions to a Welfare Plan Trust
(a) Description of Transaction. An employer receives directly from participants or withholds from employees' paychecks certain amounts that the employer forwards to a trust maintained to provide, through
insurance or otherwise, group health or other welfare benefits. The employer fails to forward such amounts in accordance with the terms of the plan or the requirements of the Department's regulation at 29 CFR 2510.3-102. There are no instances in which claims have been denied under the plan, nor has there been any lapse in coverage, due to the failure to transmit participant contributions on a timely basis.

(b) Correction of Transaction. (1) Unpaid Contributions. Pay to the Trust (1) the Principal Amount, and, where applicable, pay any penalties, late fees or other charges necessary to prevent a lapse in coverage due to the failure to make timely payments, and (2) pay to the trust the greater of (i) Lost Earnings on the Principal Amount or (ii) Restoration of Profits resulting from the employer's use of the Principal Amount as described in Section 5(b). The Principal Amount is the amount of delinquent participant contributions. The Loss Date for such contributions is the date on which each contribution would become plan assets under 29 CFR 2510.3-102. Any penalties, late fees or other charges shall be paid by the employer and not from participant contributions.

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EXHIBIT 3 Adoption of Voluntary Fiduciary Correction Program [03/28/2002], Continued

(2) Late Contributions. If participant contributions were remitted to the trust outside of the time period required by the regulation, the only correction required is to pay to the trust the greater of (i) Lost Earnings or (ii) Restoration of Profits resulting from the employer's use of the Principal Amount as described in Section 5(b). Any penalties, late fees or other such charges shall be paid by the employer and not from participant contributions.

(c) Documentation. In addition to the documentation required by Section 6, submit the following documents:

(1) For participant contributions received directly from participants, a copy of the accounting records which identify the date and amount of each contribution received;

(2) For participant contributions withheld from employees' paychecks, a copy of the payroll documents showing the date and amount of each withholding;

(3) A statement from a Plan Official identifying the earliest date on which the participant contributions reasonably could have been segregated from the employer's general assets, along with the supporting documentation on which the Plan Official relied in reaching this conclusion; and

(4) A statement from a Plan Official attesting that there are no instances in which claims have been denied under the plan for nonpayment, nor has there been any lapse in coverage.

B. Loans

1. Loan at Fair Market Interest Rate to a Party in Interest With Respect to the Plan

(a) Description of Transaction. A plan made a loan to a party in interest at an interest rate no less than that for loans with similar terms (for example, the amount of the loan, amount and type of security, repayment schedule, and duration of loan) to a borrower of similar creditworthiness. The loan was not exempt from the prohibited transaction provisions of Title I of ERISA.

(b) Correction of Transaction. Pay off the loan in full, including any prepayment penalties. An independent commercial lender must also confirm in writing that the loan was made at a fair market interest rate for a loan with similar terms to a borrower of similar creditworthiness.

(c) Documentation. In addition to the documentation required by Section 6, submit a narrative describing the process used to determine the fair market interest rate at the time the loan was made, validated in writing by an independent commercial lender.

2. Loan at Below-Market Interest Rate to a Party in Interest With Respect to the Plan

(a) Description of Transaction. A plan made a loan to a party in interest with respect to the plan at an interest rate which, at the time the loan was made, was less than the fair market interest rate for loans with similar terms (for example, the amount of loan, amount and type of security, repayment schedule, and duration of the loan) to a borrower of similar creditworthiness. The loan was not exempt from the prohibited transaction provisions of Title I of ERISA.

(b) Correction of Transaction. Pay off the loan in full, including any prepayment penalties. (1) Pay to the plan the Principal Amount, plus the greater of (i) the Lost Earnings as described in Section 5(b), or (ii) the Restoration of Profits, if any, as described in Section 5(b).

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EXHIBIT 3 Adoption of Voluntary Fiduciary Correction Program [03/28/2002], Continued

(2) For purposes of this transaction, the Principal Amount is equal to the excess of the interest payments that would have been received if the loan had been made at the fair market interest rate (from the beginning of the loan until the Recovery Date) over interest payments actually received under the loan terms during such period. For purposes of the VFC Program, the fair market interest rate must be determined by an independent commercial lender.

Example: The plan made to a party in interest a $150,000 mortgage loan, secured by a first Deed of Trust, at a fixed interest rate of 4% per annum. The loan was to be fully amortized over 30 years. The fair market interest rate for comparable loans, at the time this loan was made, was 7% per annum. The party in interest or Plan Official must repay the loan in full plus any applicable prepayment penalties. The party in interest or Plan Official also must pay the difference between what the plan would have received through the Recovery Date had the loan been made at 7% and what, in fact, the plan did receive from the commencement of the loan to the Recovery Date, plus lost earnings on that amount as described in Section 5(b).

(c) Documentation. In addition to the documentation required by Section 6, submit the following documents:

(1) a narrative describing the process used to determine the fair market interest rate at the time the loan was made;

(2) a copy of the independent commercial lender's fair market interest rate determination(s); and

(3) a copy of the independent fiduciary's dated, written approval of the fair market interest rate determination(s).

3. Loan at Below-Market Interest Rate to a Person Who Is Not a Party in Interest With Respect to the Plan

(a) Description of Transaction. A plan made a loan to a person who is not a party in interest with respect to the plan at an interest rate which, at the time the loan was made, was less than the fair market interest rate for loans with similar terms (for example, the amount of loan, amount and type of security, repayment schedule, and duration of the loan) to a borrower of similar creditworthiness.

(b) Correction of Transaction. (1) Pay to the plan the Principal Amount, plus Lost Earnings through the Recovery Date, as described in Section 5(b).

(2) Each loan payment has a Principal Amount equal to the excess of (a) interest payments that would have been received until the Recovery Date if the loan had been made at the fair market interest rate over (b) the interest actually received under the loan terms. The fair market interest rate must be determined by an independent commercial lender.

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EXHIBIT 3 Adoption of Voluntary Fiduciary Correction Program [03/28/2002], Continued

(3) From the inception of the loan to the Recovery Date, the amount to be paid to the plan is the Lost Earnings on the series of Principal Amounts, calculated in accordance with Section 5(b).

(4) From the Recovery Date to the maturity date of the loan, the amount to be paid to the plan is the present value of the remaining Principal Amounts, as determined by an independent commercial lender. Instead of calculating the present value, it is acceptable for administrative convenience to pay the sum of the remaining Principal Amounts.

(5) The principles of this paragraph (b) are illustrated in the following example:

Example: The plan made a $150,000 mortgage loan, secured by a first Deed of Trust, at a fixed interest rate of 4% per annum. The loan was to be fully amortized over 30 years. The fair market interest rate for comparable loans, at the time this loan was made, was 7% per annum. The borrower or the Plan Official must pay the excess of what the plan would have received through the Recovery Date had the loan been made at 7% over what, in fact, the plan did receive from the commencement of the loan to the Recovery Date, plus Lost Earnings on that amount as described in Section 5(b). The Plan Official must also pay on the Recovery Date the difference in the value of the remaining payments on the loan between the 7% and the 4% for the duration of the time the plan is owed repayments on the loan.

(c) Documentation. In addition to the documentation required by Section 6, submit the following documents:

(1) A narrative describing the process used to determine the fair market interest rate at the time the loan was made; and

(2) A copy of the independent commercial lender's fair market interest rate determination(s).

4. Loan at Below-Market Interest Rate Solely Due to a Delay in Perfecting the Plan's Security Interest

(a) Description of Transaction. For purposes of the VFC Program, if a plan made a purportedly secured loan to a person who is not a party in interest with respect to the plan, but there was a delay in recording or otherwise perfecting the plan's interest in the loan collateral, the loan will be treated as an unsecured loan until the plan's security interest was perfected.

(b) Correction of Transaction. (1) Pay to the plan the Principal Amount, plus Lost Earnings as described in Section 5(b), through the date the loan became fully secured.

(2) The Principal Amount is equal to the difference between (a) interest payments actually received under the loan terms and (b) the interest payments that would have been received if the loan had been made at the fair market interest rate for an unsecured loan. The fair market interest rate must be determined by an independent commercial lender.

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(3) In addition, if the delay in perfecting the loan's security caused a permanent change in the risk characteristics of the loan, the fair market interest rate for the remaining term of the loan must be determined by an independent commercial lender. In that case, the correction amount includes an additional payment to the plan. The amount to be paid to the plan is the present value of the remaining Principal Amounts from the date the loan is fully secured to the maturity date of the loan. Instead of calculating the present value, it is acceptable for administrative convenience to pay the sum of the remaining Principal Amounts.
(4) The principles of this paragraph (b) are illustrated in the following examples:

Example 1: The plan made a mortgage loan, which was supposed to be secured by a Deed of Trust. The plan's Deed was not recorded for six months, but, when it was recorded, the Deed was in first position. The interest rate on the loan was the fair market interest rate for a mortgage loan secured by a first-position Deed of Trust. The loan is treated as an unsecured, below-market loan for the six months prior to the recording of the Deed of Trust.
Example 2: Assume the same facts as in Example 1, except that, as a result of the delay in recording the Deed, the plan ended up in second position behind another lender. The risk to the plan is higher and the interest rate on the note is no longer commensurate with that risk. The loan is treated as a below-market loan (based on the lack of security) for the six months prior to the recording of the Deed of Trust and as a below-market loan (based on secondary status security) from the time the Deed is recorded until the end of the loan.

(c) Documentation. In addition to the documentation required by Section 6, submit the following documents:
(1) A narrative describing the process used to determine the fair market interest rate for the period that the loan was unsecured and, if applicable, for the remaining term of the loan; and
(2) A copy of the independent commercial lender's fair market interest rate determination(s).

C. Purchases, Sales and Exchanges

1. Purchase of an Asset (Including Real Property) by a Plan From a Party in Interest

(a) Description of Transaction. A plan purchased an asset with cash from a party in interest with respect to the plan, and under the circumstances, no prohibited transaction exemption applies.

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EXHIBIT 3 Adoption of Voluntary Fiduciary Correction Program [03/28/2002], Continued

(b) Correction of Transaction. (1) The transaction must be corrected by the sale of the asset back to the party in interest who originally sold the asset to the plan or to a person who is not a party in interest. Whether the asset is sold to a person who is not a party in interest with respect to the plan or is sold back to the original seller, the plan must receive the higher of (i) the fair market value (FMV) of the asset at the time of resale, without a reduction for the costs of sale; or (ii) the Principal Amount, plus the greater of (A) Lost Earnings on the Principal Amount as described in Section 5(b), or (B) the Restoration of Profits, if any, as described in Section 5(b).

(2) For this transaction, the Principal Amount is the plan's original purchase price.

(3) The principles of this paragraph (b) are illustrated in the following example:

Example: A plan purchased from the plan sponsor a parcel of real property. The plan does not lease the property to any person. Instead, the plan uses the property as an office. The Plan Official obtains from a qualified, independent appraiser an appraisal of the property reflecting the FMV of the property at the time of purchase. The appraiser values the property at $100,000, although the plan paid the plan sponsor $120,000 for the property. As of the Recovery Date the property is valued at $110,000. To correct the transaction, the plan sponsor repurchases the property for $120,000 with no reduction for the costs of sale and reimburses the plan for the initial costs of sale. The plan sponsor also must pay the plan the greater of the plan's Lost Earnings or the sponsor's profits on this amount. This example assumes that the plan sponsor did not make a profit on the $120,000 proceeds from the original sale of the property to the plan.

(c) Documentation. In addition to the documentation required by Section 6, submit the following documents:

(1) Documentation of the plan's purchase of the real property, including the date of the purchase, the plan's purchase price, and the identity of the seller;

(2) A narrative describing the relationship between the original seller of the asset and the plan; and

(3) The qualified, independent appraiser's report addressing the FMV of the asset purchased by the plan, both at the time of the original purchase and at the recovery date.

2. Sale of an Asset (Including Real Property) by a Plan to a Party in Interest

(a) Description of Transaction. A plan sold an asset for cash to a party in interest with respect to the plan, in a transaction that is not exempt from the prohibited transaction provisions of Title I of ERISA.

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(b) Correction of Transaction. (1) The plan must receive the Principal Amount plus the greater of (i) Lost Earnings as described in Section 5(b), or (ii) the Restoration of Profits, if any, as described in Section 5(b). As an alternative to repayment of the Principal Amount, if it is determined that the plan will realize a greater benefit by repurchasing the asset, the plan may repurchase the asset from the party in interest \12\ at the lower of the price for which it sold the property or the FMV of the property as of the Recovery Date plus restoration to the plan of the party in interest's net profits from owning the property, to the extent they exceed the plan's investment return from the proceeds of the sale. The determination as to which correction alternative the plan chooses must be made by an independent fiduciary.

\12\ The repurchase of the same property from the party in interest to whom the asset was sold is a reversal of the original prohibited transaction. The sale is not a new prohibited transaction and therefore does not require an exemption.

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EXHIBIT 3 Adoption of Voluntary Fiduciary Correction Program [03/28/2002], Continued

(2) For this transaction, the Principal Amount is the amount by which the FMV of the asset (at the time of the original sale) exceeds the sale price.
(3) The principles of this paragraph (b) are illustrated in the following example:

Example: A plan sold a parcel of unimproved real property to the plan sponsor. The sponsor did not make any profit on the use of the property. The Plan Official obtains from a qualified, independent appraiser an appraisal of the property reflecting the FMV of the property as of the date of sale. The appraiser valued the property at $130,000, although the plan sold the property to the plan sponsor for $120,000. However, the plan fiduciaries have reason to believe that the property will substantially increase in the near future based on the anticipated building of a shopping mall adjacent to the property in question and, as of the Recovery Date, the appraiser values the property at $140,000. An independent fiduciary determines that the property is a prudent investment for the plan, and will not result in any liquidity or diversification problems. The plan corrects by repurchasing the property at the original sale price, with the party in interest assuming the costs of the reversal of the sale transaction.

(c) Documentation. In addition to the documentation required by Section 6, submit the following documents:
(1) Documentation of the plan's sale of the asset, including the date of the sale, the sales price, and the identity of the original purchaser;
(2) A narrative describing the relationship of the purchaser to the asset and the relationship of the purchaser to the plan;
(3) The qualified, independent appraiser's report addressing the FMV of the property at the time of the sale from the plan and as of the Recovery Date; and
(4) The independent fiduciary's report that the property is a prudent investment for the plan.

3. Sale and Leaseback of Real Property to Employer
(a) Description of Transaction. The plan sponsor sold a parcel of real property to the plan, which then was leased back to the sponsor, in a transaction that is not otherwise exempt.
(b) Correction of Transaction. (1) The transaction must be corrected by the sale of the parcel of real property back to the plan sponsor or to a person who is not a party in interest with respect to the plan.\13\ The plan must receive the higher of (i) FMV of the asset at the time of resale, without a reduction for the costs of sale; or (ii) the Principal Amount, plus the greater of (A) Lost Earnings on the Principal Amount as described in Section 5(b), or (B) the Restoration of Profits, if any, as described in Section 5(b).

\13\ If the plan purchased the property from the plan sponsor, the sale of the same property back to the plan sponsor is a reversal of the prohibited transaction. The sale is not a new prohibited transaction and therefore does not require an individual prohibited transaction exemption, as long as the plan did not make improvements while it owned the property.

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EXHIBIT 3 Adoption of Voluntary Fiduciary Correction Program [03/28/2002], Continued

(2) If the plan has not been receiving rent at FMV, as determined by a qualified, independent appraisal, the sale price of the real property should not be based on the historic below-market rent that was paid to the plan.

(3) In addition to the correction amount in subparagraph (1), if the plan was not receiving rent at FMV, as determined by a qualified, independent appraiser, the Principal Amount also includes the difference between the rent actually paid and the rent that should have been paid at FMV. The plan sponsor must pay to the plan this additional Principal Amount, plus the greater of (i) Lost Earnings or (ii) Restoration of Profits resulting from the plan sponsor's use of the Principal Amount, as described in Section 5(b).

(4) The principles of this paragraph (b) are illustrated in the following example:

Example: The plan purchased at FMV from the plan sponsor an office building that served as the sponsor's primary business site. Simultaneously, the plan sponsor leased the building from the plan at below the market rental rate. The Plan Official obtains from a qualified, independent appraiser an appraisal of the property reflecting the FMV of the property and rent. To correct the transaction, the plan sponsor purchases the property from the plan at the higher of the appraised value at the time of the resale or the original sales price and also pays the Lost Earnings. Because the rent paid to the plan was below the market rate, the sponsor must also make up the difference between the rent paid under the terms of the lease and the amount that should have been paid, plus Lost Earnings on this amount, as described in Section 5(b).

(c) Documentation. In addition to the documentation required by Section 6, submit the following documents:

(1) Documentation of the plan's purchase of the real property, including the date of the purchase, the plan's purchase price, and the identity of the original seller;

(2) Documentation of the plan's sale of the asset, including the date of sale, the sales price, and the identity of the purchaser;

(3) A narrative describing the relationship of the original seller to the plan and the relationship of the purchaser to the plan;

(4) A copy of the lease;

(5) Documentation of the date and amount of each lease payment received by the plan; and

(6) The qualified, independent appraiser's report addressing both the FMV of the property at the time of the original sale and at the Recovery Date, and the FMV of the lease payments.

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EXHIBIT 3 Adoption of Voluntary Fiduciary Correction Program [03/28/2002], Continued

4. Purchase of an Asset (Including Real Property) by a Plan From a Person Who Is Not a Party in Interest With Respect to the Plan at a Price Other Than Fair Market Value

(a) Description of Transaction. A plan acquired an asset from a person who is not a party in interest with respect to the plan, without determining the asset's FMV. As a result, the plan paid more than it should have for the asset.

(b) Correction of Transaction. The Principal Amount is the difference between the actual purchase price and the asset's FMV at the time of purchase. The plan must receive the Principal Amount plus the Lost Earnings, as described in Section 5(b).

(1) The principles of this paragraph (b) are illustrated in the following example:

Example: A plan bought unimproved land without obtaining a qualified, independent appraisal. Upon discovering that the purchase price was $10,000 more than the appraised FMV, the Plan Official pays the plan the Principal Amount of $10,000, plus Lost Earnings as described in Section 5(b).

(c) Documentation. In addition to the documentation required by Section 6, submit the following documents:

(1) Documentation of the plan's original purchase of the asset, including the date of the purchase, the purchase price, and the identity of the seller;

(2) A narrative describing the relationship of the seller to the plan; and

(3) A copy of the qualified, independent appraiser's report addressing the FMV at the time of the plan's purchase.

5. Sale of an Asset (Including Real Property) By a Plan to a Person Who Is Not a Party in Interest With Respect to the Plan at a Price Less Than Fair Market Value

(a) Description of Transaction. A plan sold an asset to a person who is not a party in interest with respect to the plan, without determining the asset's FMV. As a result, the plan received less than it should have from the sale.

(b) Correction of Transaction. The Principal Amount is the amount by which the FMV of the asset as of the Recovery Date exceeds the price at which the plan sold the property. The plan must receive the Principal Amount plus Lost Earnings as described in Section 5(b).

(1) The principles of this paragraph (b) are illustrated in the following example:

Example: A plan sold unimproved land without taking steps to ensure that the plan received FMV. Upon discovering that the sale price was $10,000 less than the FMV, the Plan Official pays the plan the Principal Amount of $10,000 plus Lost Earnings as described in Section 5(b).

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EXHIBIT 3 Adoption of Voluntary Fiduciary Correction Program [03/28/2002], Continued

(c) Documentation. In addition to the documentation required by Section 6, submit the following documents:

(1) Documentation of the plan's original sale of the asset, including the date of the sale, the sale price, and the identity of the buyer;

(2) A narrative describing the relationship of the buyer to the plan; and

(3) A copy of the qualified, independent appraiser's report addressing the FMV at the time of the plan's sale.

D. Benefits

1. Payment of Benefits Without Properly Valuing Plan Assets on Which Payment is Based

(a) Description of Transaction. A defined contribution pension plan pays benefits based on the value of the plan's assets. If one or more of the plan's assets are not valued at current value, the benefit payments are not correct. If the plan's assets are overvalued, the current benefit payments will be too high. If the plan's assets are undervalued, the current benefit payments will be too low.

(b) Correction of Transaction. (1) Establish the correct value of the improperly valued asset for each plan year, starting with the first plan year in which the asset was improperly valued. Restore to the plan for distribution to the affected plan participants, or restore directly to the plan participants, the amount by which all affected participants were underpaid distributions to which they were entitled under the terms of the plan, plus the higher of Lost Earnings or the underpayment rate defined in Section 6621(a)(2) of the Code on the underpaid distributions. File amended Annual Report Forms 5500, as detailed below.

(2) To correct the valuation defect, a Plan Official must determine the FMV of the improperly valued asset per Section 5(a) for each year in which the asset was valued improperly.

(3) Once the FMV has been determined, the participant account balances for each year must be adjusted accordingly.

(4) The Annual Report Forms 5500 must be amended and refiled for (i) the last three plan years or (ii) all plan years in which the value of the asset was reported improperly, whichever is less.

(5) The Plan Official or plan administrator must determine who received distributions from the plan during the time the asset was valued improperly. For distributions that were too low, the amount of the underpayment is treated as a Principal Amount for each individual who received a distribution. The Principal Amount and Lost Earnings must be paid to the affected individuals. For distributions that were too high, the total of the overpayments constitutes the Principal Amount for the plan. The Principal Amount plus the Lost Earnings, as described in Section 5(b), must be restored to the plan or to any participants who received distributions that were too low.

(6) The principles of this paragraph (b) are illustrated in the following examples:

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EXHIBIT 3 Adoption of Voluntary Fiduciary Correction Program [03/28/2002], Continued

Example 1. On December 31, 1995, a profit sharing plan purchased a 20-acre parcel of real property for $500,000, which represented a portion of the plan's assets. The plan has carried the property on its books at cost, rather than at FMV. One participant left the company on January 1, 1997, and received a distribution, which included her portion of the value of the property. The separated participant's account balance represented 2% of the plan's assets. As part of correction for the VFC Program, a qualified, independent appraiser has determined the FMV of the property for 1996, 1997, and 1998. The FMV as of December 31, 1996, was $400,000. Therefore, this participant was overpaid by $2,000 (($500,000-$400,000) multiplied by 2%). The Plan Officials corrected the transaction by paying to the plan $2,500, consisting of $2,000 Principal Amount and $500 Lost Earnings. The Lost Earnings were based on a return of 25%, which represents the total return on the plan's investments from the date of the distribution to the participant until the date of correction.

The plan administrator also filed an amended Form 5500 for plan years 1996 and 1997, to reflect the proper values. The plan administrator will include the correct asset valuation in the 1998 Form 5500 when that form is filed.

Example 2. Assume the same facts as in Example 1, except that the property had appreciated in value to $600,000 as of December 31, 1996. The separated participant would have been underpaid by $2,000. The correction consists of locating the participant and distributing $2,500 to her ($2,000 Principal Amount and $500 Lost Earnings), as well as filing the amended Forms 5500.

(c) Documentation. In addition to the documentation required by Section 6, submit the following documents:

(1) A copy of the qualified, independent appraiser's report for each plan year in which the asset was revalued;

(2) A written statement confirming the date that amended Annual Report Forms 5500 with correct valuation data were filed;

(3) If losses are restored to the plan, proof of payment to the plan and copies of the adjusted participant account balances; and

(4) If supplemental distributions are made, proof of payment to the individuals entitled to receive the supplemental distributions.

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EXHIBIT 3 Adoption of Voluntary Fiduciary Correction Program [03/28/2002], Continued

E. Plan Expenses

1. Duplicative, Excessive, or Unnecessary Compensation Paid by a Plan

(a) Description of Transaction. A plan paid excessive compensation, including commissions or fees, to a service provider (such as an attorney, accountant, actuary, financial advisor, or insurance agent); a plan paid two or more persons to provide the same services to the plan; or a plan paid a service provider for services that were not necessary for the operation of the plan.

(b) Correction of Transaction. (1) Restore to the plan the Principal Amount, plus the greater of (i) Lost Earnings or (ii) Restoration of Profits resulting from the use of the Principal Amount, as described in Section 5(b).

(2) The Principal Amount is the difference between (a) the amount actually paid by the plan to the service provider during the six years prior to the discontinuation of the payment of the excessive, duplicative, or unnecessary compensation and (b) the reasonable market value of the non-duplicative services.

(3) The principles of this paragraph (b) are illustrated in the following example:

Example. Excessive compensation. A plan hired an investment advisor who advised the plan's trustees about how to invest the plan's entire portfolio. In accordance with the plan document, the trustees instructed the advisor to limit the plan's investments to equities and bonds. In exchange for his services, the plan paid the investment advisor 3% of the value of the portfolio's assets. If the trustees had inquired they would have learned that comparable investment advisors charged 1% of the value of the assets for the type of portfolio that the plan maintained. To correct the transaction, the plan must be paid the Principal Amount of 2% of the value of the plan's assets, plus Lost Earnings, as described in Section 5(b).

(c) Documentation. In addition to the documentation required by Section 6, submit the following documents:

(1) A written estimate of the reasonable market value of the services;

(2) The estimator's qualifications; and

(3) The cost of the services at issue during the period that such services were provided to the plan.

2. Payment of Dual Compensation to a Plan Fiduciary

(a) Description of Transaction. A plan pays a fiduciary for services rendered to the plan when the fiduciary already receives full-time pay from an employer or an association of employers, whose employees are participants in the plan, or from an employee organization whose members are participants in the plan. The plan's payments to the plan fiduciary are not mere reimbursements of expenses properly and actually incurred by the fiduciary.

(b) Correction of Transaction. (1) Restore to the plan the Principal Amount, plus the greater of (i) Lost Earnings or (ii) Restoration of Profits resulting from the fiduciary's use of the Principal Amount for the same period.

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(2) The Principal Amount is the difference between (a) the amount actually paid by the plan during the six years prior to the discontinuation of the payments to the fiduciary and (b) the amount that represents reimbursements of expenses properly and actually incurred by the fiduciary.

(3) The principles of this paragraph (b) are illustrated in the following example:

Example. A union sponsored a health plan funded through contributions by employers. The union president receives $50,000 per year from the union in compensation for his services as union president. He is appointed as a trustee of the health plan while retaining his position as union president. In exchange for acting as plan trustee, the union president is paid a salary of $200 per week by the plan while still receiving the $50,000 salary from the union. Since $50,000 is full-time pay, the plan's weekly salary payments are improper. To correct the transaction, the plan must be paid the Principal Amount, which is the $200 weekly salary amount for each week that the salary was paid, plus the higher of Lost Earnings or Restoration of Profits, as described in Section 5(b).

(c) Documentation. In addition to the documentation required by Section 6, submit the following documents:

(1) Copies of the plan's accounting records which show the date and amount of compensation paid by the plan to the identified fiduciary; and

(2) If any of the amounts paid by the plan to the fiduciary represent reimbursements of expenses properly and actually incurred by the fiduciary, include copies of the plan records which indicate the date, amount, and character of these payments.

Signed at Washington, DC this 25th day of March, 2002.
Ann L. Combs,
Assistant Secretary for Pension and Welfare Benefits Administration,
U.S. Department of Labor.
Appendix A.--Sample VFC Program No Action Letter

Continued on next page

EXHIBIT 3 Adoption of Voluntary Fiduciary Correction Program [03/28/2002], Continued

Applicant (Plan Official)

Address

Dear Applicant (Plan Official):

Re: VFC Program Application No. xx-xxxxxx

The Department of Labor, Pension and Welfare Benefits Administration (PWBA), has responsibility for administration and enforcement of Title I of the Employee Retirement Income Security Act of 1974, as amended (ERISA). PWBA has established a Voluntary Fiduciary Correction Program to encourage the correction of breaches of fiduciary responsibility and the restoration of losses to the plan participants and beneficiaries.

In accordance with the requirements of the VFC Program, you have identified the following transactions as breaches, or potential breaches, of Part 4 of Title I of ERISA, and you have submitted documentation to PWBA that demonstrates that you have taken the corrective action indicated.

[Briefly recap the violation and correction. Example: Failure to deposit participant contributions to the XYZ Corp. 401(k) plan within the time frames required by ERISA, from ______ (date) to ______ (date). All participant contributions were deposited by ______ (date) and lost earnings on the delinquent contributions were deposited and allocated to participants' plan accounts on ______ (date).]

Because you have taken the above-described corrective action that is consistent with the requirements of the VFC Program, PWBA will take no civil enforcement action against you with respect to this breach. Specifically, PWBA will not recommend that the Solicitor of Labor initiate legal action against you, and PWBA will not impose the penalty in section 502(l) of ERISA on the amount you have repaid to the plan.

PWBA's decision to take no further action is conditioned on the completeness and accuracy of the representations made in your application. You should note that this decision will not preclude PWBA from conducting an investigation of any potential violations of criminal law in connection with the transaction identified in the application or investigating the transaction identified in the application with a view toward seeking appropriate relief from any other person.

Continued on next page

EXHIBIT 3 Adoption of Voluntary Fiduciary Correction Program [03/28/2002], Continued

[If the transaction is a prohibited transaction for which no exemptive relief is available, add the following language: Please also be advised that pursuant to section 3003(c) of ERISA, 29 U.S.C. section 1203(c), the Secretary of Labor is required to transmit to the Secretary of the Treasury information indicating that a prohibited transaction has occurred. Accordingly, this matter will be referred to the Internal Revenue Service.]

In addition, you are cautioned that PWBA's decision to take no further action is binding on PWBA only. Any other governmental agency, and participants and beneficiaries, remain free to take whatever action they deem necessary.

If you have any questions about this letter, you may contact the Regional VFC Program Coordinator at applicable address and telephone number.

Appendix B.--VFC Program Checklist

Use this checklist to ensure that you are submitting a complete application. The applicant must sign and date the checklist and include it with the application. Indicate ``Yes", ``No" or ``N/A" next to each item. A ``No" answer or the failure to include a completed checklist will delay review of the application until all
required items are received.

______1. Have you reviewed the eligibility, definitions, transaction and correction, and documentation sections of the VFC Program?
______ 2. Have you included the name, address and telephone number of a contact person familiar with the contents of the application?
______ 3. Have you provided the EIN # and address of the plan sponsor and plan administrator?
______ 4. Have you provided the date that the most recent Form 5500 was filed by the plan?
______ 5. Have you enclosed a signed and dated certification under penalty of perjury for each applicant and the applicant's representative, if any?
______ 6. Have you enclosed relevant portions of the plan document and any other pertinent documents (such as the adoption agreement, trust agreement, or insurance contract) with the relevant sections identified?
______ 7. Have you enclosed a statement identifying the current fidelity bond for the plan?
______ 8. Where applicable, have you enclosed a copy of an appraiser's report?
______ 9. Have you enclosed other documents as specified by the individual transactions and corrections?
______ a. A detailed narrative of the Breach, including the date it occurred;
______ b. Documentation that supports the narrative description of the transaction;
______ c. An explanation of how the Breach was corrected, by whom and when, with supporting documentation;

Continued on next page

EXHIBIT 3 Adoption of Voluntary Fiduciary Correction Program [03/28/2002], Continued

______ d. A list of all persons materially involved in the Breach and its correction (e.g., fiduciaries, service providers, borrowers, lenders);
______ e. Documentation establishing the return on the plan's other investments during the time period the plan engaged in the transaction described in the VFC Program application;
______ f. Specific calculations demonstrating how Principal Amount and Lost Earnings or Restoration of Profits were computed; and
______ g. Proof of payment of Principal Amount and Lost Earnings or Restoration of Profits.
______ 10. If you are an eligible applicant and wish to avail yourself of excise tax relief under the Proposed Class Exemption, have you made proper arrangements to provide within 60 calendar days following the date of this application a copy of the Class Exemption's required notice to all interested persons and to the PWBA regional office to which the application is filed?
______ 11. Where applicable, have you enclosed a description demonstrating proof of payment to participants and beneficiaries whose current location is known to the plan and/or applicant, and for participants who need to be located, have you described how adequate funds have been segregated to pay missing participants and commenced the process of locating the missing participants using either the IRS and Social Security Administration locator services, or other comparable means?
______ 12. Has the plan implemented measures to ensure that the transactions specified in the application do not recur? (Do not include this with the application. The Department will not opine on the adequacy of these measures.)

Signature of Applicant and Date Signed

Name of Applicant (Typed):
Title/Relationship to the Plan (Typed):
Name of Plan, EIN and Plan Number (Typed):

Appendix C.--List of PWBA Regional Offices

Continued on next page

EXHIBIT 3 Adoption of Voluntary Fiduciary Correction Program [03/28/2002], Continued

Atlanta Regional Office, 61 Forsyth Street, SW, Suite 7B54, Atlanta, GA 30303, telephone (404) 562-2156, fax (404) 562-2168; jurisdiction: Alabama, Florida, Georgia, Mississippi, North Carolina, South Carolina, Tennessee, Puerto Rico.

Boston Regional Office, J.F.K. Building, Room 575, Boston, MA 02203, telephone: (617) 565-9600, fax: (617) 565-9666; jurisdiction: Connecticut, Maine, Massachusetts, New Hampshire, central and western New York, Rhode Island, Vermont.

Chicago Regional Office, 200 West Adams Street, Suite 1600, Chicago, IL 60606, telephone (312) 353-0900, fax (312) 353-1023; jurisdiction: northern Illinois, northern Indiana,

Wisconsin.Cincinnati Regional Office, 1885 Dixie Highway, Suite 210, Ft. Wright, KY 41011-2664, telephone (859) 578-4680, fax (859) 578-4688; jurisdiction: southern Indiana, Kentucky, Michigan, Ohio.

Dallas Regional Office, 525 Griffin Street, Rm. 707, Dallas, TX 75202-5025, telephone (214) 767-6831, fax (214) 767-1055; jurisdiction: Arkansas, Louisiana, New Mexico, Oklahoma, Texas.

Kansas City Regional Office, 1100 Main Street, Suite 1200, Kansas City, MO 64105-2112, telephone (816) 426-5131, fax (816) 426-5511; jurisdiction: Colorado, southern Illinois, Iowa, Kansas, Minnesota, Missouri, Montana, Nebraska, North Dakota, South Dakota, Wyoming.

Los Angeles Regional Office, 790 E. Colorado Boulevard, Suite 514, Pasadena, CA 91101, telephone (626) 583-7862, fax (626) 583-7845; jurisdiction: 10 southern counties of California, Arizona, Hawaii, American Samoa, Guam, Wake Island.

New York Regional Office, temporarily located at 201 Varick Street, New York, NY 10014, telephone (212) 337-2228, fax (212) 337-2112; jurisdiction: southeastern New York, northern New Jersey.

Philadelphia Regional Office, The Curtis Center, 170 S. Independence Mall West, Suite 870 West, Philadelphia, PA 19106-3317, telephone 215-861-5300, fax 215-861-5347; jurisdiction: Delaware, Maryland, southern New Jersey, Pennsylvania, Virginia, Washington, D.C., West Virginia.

San Francisco Regional Office, 71 Stevenson St., Suite 915, San Francisco, CA 94105, telephone (415) 975-4600, fax (415) 975-4589; jurisdiction: Alaska, 48 northern counties of California, Idaho, Nevada, Oregon, Utah, Washington.

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EXHIBIT 3 Adoption of Voluntary Fiduciary Correction Program [03/28/2002], Continued

**Please verify current telephone numbers and addresses on PWBA's website.

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